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1999]

Note

RISKY BUSINESS: HTAs, THE CASH FORWARD EXCLUSION AND *TOP OF IOWA COOPERATIVE v. SCHEWE*

*"Buy low, sell high. Fear—that's the other guy's problem."*¹

I. INTRODUCTION

Disaster hit America's farm belt in 1995-96, affecting millions of tons of grain, bringing financial ruin to many and tearing apart the economic and social fabric of small communities across the Midwest.² This catastrophe caused losses totaling hundreds of millions of dollars.³ Ironically, this tragedy resulted not from crop failures, infestations or natural disasters, but from unprecedented movements in the grain markets that saw the price of corn more than double during that time.⁴

The reason this price rise wrought such financial havoc was the widespread use of "Flex-Hedge-To-Arrive" contracts (HTAs) between farmers and grain elevators ("elevators"), ostensibly used to protect against the risk of price drops before the parties could deliver their crops to market.⁵

1. TRADING PLACES (Paramount 1983).

2. See Tom Seery, *Heartache in Buffalo Center: Risky Grain Trading Tears Iowa Town Apart*, SAN DIEGO UNION-TRIB., July 27, 1996, at C2 (describing effects of hedge-to-arrive (HTA) contracts on small community).

3. See George Gunset, *CFTC Acts on Grain Hedging Contracts: Farmers Facing Losses Look to Government for Help*, CHICAGO TRIB., Nov. 30, 1996, at 1 (noting one individual case affecting 15 million tons of grain); David Hendee, *Hedge Contracts Sour the Harvest for Some Farmers Avoiding a Repeat*, OMAHA WORLD-HERALD, Sept. 15, 1996, at 1A, available in 1996 WL 6031027 (estimating losses over \$500 million); James Walsh, *Hurt by the Hedge: Sustained High Grain Prices Are Costly for Farmers, Coop.*, MINNEAPOLIS-ST. PAUL STAR-TRIB., Aug. 18, 1996, at 1D, available in 1996 WL 6925381 (estimating losses could reach \$500 million).

4. See *In re Grain Land Coop.*, 978 F. Supp. 1267, 1270 (D. Minn. 1997) (describing rise in corn prices beginning in October 1994); Hendee, *supra* note 3, at 1A (stating per bushel corn price rose from approximately two dollars to over five dollars).

5. See *Grain Land Coop.*, 978 F. Supp. at 1270 (describing combined effects of "unprecedented" price rise and contract terms as factors leading to elevator's financial difficulties); Nicholas P. Iavarone, *Understanding the Hedge-To-Arrive Controversy*, 2 DRAKE J. AGRIC. L. 371, 390-93, 400 (1997) (describing potentially disastrous results from using HTA contracts during 1995-96 crop years and asserting that purpose of HTAs is supposedly to provide price protection); Eric Asklesen, Note, *Hedge-To-Arrive Contracts and the Commodity Exchange Act*, 7 KAN J.L. & PUB. POL'Y 122, 123, 125 (1998) (noting HTAs are used to protect against dropping prices and asserting record-setting prices in 1996 led to financial problems for parties engaged in HTA contracts); Matthew J. Cole, Note, *Hedge-To-Arrive Contracts:*

Grain producers have long relied on "cash forward" contracts to guarantee a fixed price for crops that are to be delivered at a later date.⁶ HTA contracts are more flexible variants of cash forward contracts.⁷ Cash forward contracts are designed to protect farmers from adverse price changes and to secure grain dealers a source of supply.⁸ HTAs are intended to provide similar protections and also enable grain producers to take advantage of short-term fluctuations in the market.⁹ This greater degree of flexibility also introduces more opportunities for speculation and accordingly leads to an equivalently increased level of financial exposure.¹⁰ The risks inherent in HTAs made farmers and elevators particularly vulnerable to the rising prices from 1995 to 1996.¹¹

The Second Chapter of the Farm Crisis, 1 DRAKE J. AGRIC. L. 243, 249 (1996) (stating HTAs originated in response to predictably lower grain market at harvest and resulting demand for contract capable of stabilizing revenue). HTA contracts come in a wide variety. See *Barz v. Geneva Elevator Co.*, 12 F. Supp. 2d 943, 945 (N.D. Iowa 1998) (asserting HTAs are widely varied in terms of language and parties' circumstances); *Top of Iowa Coop. v. Schewe*, 6 F. Supp. 2d 843, 846 (N.D. Iowa 1998) (acknowledging terms of HTAs differ in each case); Asklesen, *supra*, at 125 (briefly describing variety of HTA contracts). For purposes of simplicity, this Note will use the term "HTA" to refer to more speculative and complex variations (including Flex-HTAs) and will distinguish simple versions when necessary.

6. See ROBERT W. KOLB, UNDERSTANDING FUTURES MARKETS 2-3 (1987) (defining forward contract and noting theories on origins); JERRY W. MARKHAM, THE HISTORY OF COMMODITY FUTURES TRADING AND ITS REGULATION 3 (1987) (describing use of to arrive or forward contracts to protect against seasonal price drops in grain markets); Iavarone, *supra* note 5, at 372 (describing purposes and traditional methods of "hedging" in forward contracts). Forward contracts are typically defined as "a cash sale of physical commodities for deferred shipment or delivery." Asklesen, *supra* note 5, at 123.

7. See *Grain Land Coop.*, 978 F. Supp. at 1269 (characterizing HTAs as variant of "fixed-price contract for deferred delivery" with flexible pricing and delivery terms); Iavarone, *supra* note 5, at 373-74 (describing simple HTA contract); Cole, *supra* note 5, at 248 (describing HTA contracts as variations on forward pricing contracts).

8. See MARKHAM, *supra* note 6, at 3 (describing functions of to arrive contracts); Iavarone, *supra* note 5, at 372-73 (describing purposes and traditional methods of hedging); Lewis D. Solomon & Howard B. Dicker, *The Crash of 1987: A Legal and Public Policy Analysis*, 57 FORDHAM L. REV. 191, 194 (1988) (asserting that "[f]orward contracts enabled farmers to secure a specific price while allowing distributors and processors to obtain a guaranteed supply of the commodity").

9. See *Grain Land Coop.*, 978 F. Supp. at 1269 (discussing features of HTAs); *Countrymark Coop., Inc. v. Smith*, No. 5-97-21, 1997 WL 762813, at *3 (Ohio Ct. App. Dec. 8, 1997) (describing benefits of HTAs in providing greater flexibility and enabling farmers to protect against usual downturn in prices at harvest time).

10. See *Grain Land Coop.*, 978 F. Supp. at 1270 (asserting parties' course of performance under HTAs created financial problems for Grain Land); *Countrymark*, 1997 WL 762813, at *3 (asserting greater flexibility of flex-HTAs also leads to greater risk).

11. See Asklesen, *supra* note 5, at 126 (stating price rises in corn market led to increased financial risk for elevators engaged in HTAs that permitted rolling scheduled deliveries to new reference month).

The economic and legal consequences of the 1995-96 price rise are still unresolved.¹² Parties seeking to avoid their obligations under HTAs have argued a number of theories ranging from RICO and federal securities violations, to common law fraud, breach of fiduciary duty and negligent misrepresentation.¹³ The most contentious issue, however, is whether HTAs are valid cash forward contracts or "futures" contracts that can be traded only on exchanges subject to Commodity Futures Trading Commission ("CFTC") regulation.¹⁴ In a series of opinions issued during the spring and summer of 1998, Judge Bennett of the United States District Court for the Northern District of Iowa addressed this issue and ruled that the individual HTAs involved were valid "cash forward" contracts that were beyond the regulatory reach of the CFTC.¹⁵

This Note discusses the Northern District of Iowa's ruling in *Top of Iowa Cooperative v. Schewe*¹⁶ in light of other decisions regarding the regulation of contracts for future delivery of commodities.¹⁷ Part II analyzes and compares cash forward contracts, futures contracts and HTAs in terms of how each functions and the purposes each serves.¹⁸ Part II also summarizes the history and goals of commodity regulation and the manner in which courts have treated the "cash forward exclusion" of the Commodity Exchange Act (CEA).¹⁹ Part III discusses the relevant facts of *Top of Iowa*.²⁰ Part IV traces the district court's approach in determining if the

12. See Anne Fitzgerald, *Disputes Linger Over Hedge-To-Arrive Grain Contracts*, DES MOINES REG., Apr. 19, 1998, at 1, available in 1998 WL 3203515 (describing ongoing conflicts prompted by corn price increase).

13. See *Barz v. Geneva Elevator Co.*, 12 F. Supp. 2d 943, 957-59 (N.D. Iowa 1998) (alleging negligent misrepresentation); *Top of Iowa Coop. v. Schewe*, 6 F. Supp. 2d 843, 850 (N.D. Iowa 1998) (alleging securities violations); *Oeltjenbrun v. CSA Investors, Inc.*, 3 F. Supp. 2d 1024, 1052-53 (N.D. Iowa 1998) (alleging breach of fiduciary duty); *Eby v. Producers Co-op., Inc.*, 959 F. Supp. 428, 430 (W.D. Mich. 1997) (alleging RICO violations); *Grain Land Coop.*, 978 F. Supp. at 1279 (alleging common law fraud, material misrepresentation and negligent misrepresentation).

14. See *Top of Iowa*, 6 F. Supp. 2d at 846 (describing issue as "the key question in almost all of the cases involving HTAs"); *Oeltjenbrun*, 3 F. Supp. 2d at 1027 (describing issue of whether HTAs are cash forward or futures contracts as "highly contentious" and "fundamental").

15. See *Johnson v. Land O'Lakes, Inc.*, 18 F. Supp. 2d 985, 1001 (N.D. Iowa 1998) (concluding HTAs in question were valid cash forward contracts); *Barz*, 12 F. Supp. 2d at 957 (same); *Top of Iowa*, 6 F. Supp. 2d at 858 (same); *Oeltjenbrun*, 3 F. Supp. 2d at 1041-42, 1044, 1047 (same).

16. 6 F. Supp. 2d 843 (N.D. Iowa 1998).

17. For a discussion of the facts of the case and an analysis of the court's reasoning, see *infra* notes 106-87 and accompanying text. For a discussion of significant cases addressing the distinction between futures and cash forward contracts, see *infra* notes 79-105 and accompanying text.

18. For a discussion of the types of contracts at issue, see *infra* notes 23-78 and accompanying text.

19. 7 U.S.C. §§ 1-25 (1994 & Supp. 1995). For a further discussion of the major cases addressing the cash forward exclusion, see *infra* notes 79-105 and accompanying text.

20. For a discussion of the facts of *Top of Iowa*, see *infra* notes 106-16 and accompanying text.

HTAs in question were valid cash forward contracts and also analyzes the conclusions of law of the district court's decision.²¹ Last, Part V discusses the likely impact of the district court's decision regarding the validity of HTAs and how problems related to HTAs might be addressed in the future.²²

II. BACKGROUND

A. *Cash Forward Contracts, Futures and the "Cash Forward Exclusion" of the Commodity Exchange Act*

In a cash forward contract, the commodity purchaser pays a fixed price for a certain quantity of the commodity to be delivered at a set time in the future.²³ Both parties contemplate actual delivery, and ultimate delivery is an obligation of the seller under the contract.²⁴ This arrangement enables a farmer to secure a price for crops long before they are harvested, or even planted, and provides the buyer with a reasonably guaranteed source of supply to be delivered at a specific time.²⁵ Although

21. For a discussion and analysis of the court's reasoning, see *infra* notes 117-87 and accompanying text.

22. For a discussion of the outlook for the future of HTAs and the possibility of their regulation, see *infra* notes 188-215 and accompanying text.

23. See Cole, *supra* note 5, at 247 ("A forward contract is a cash sale of physical commodities for deferred shipment or delivery.").

24. See *Commodity Futures Trading Comm'n v. Noble Metals Int'l, Inc.*, 67 F.3d 766, 772 (9th Cir. 1995) (stating parties to cash forward contracts contemplate and intend future delivery of actual commodity); *Salomon Forex, Inc. v. Tauber*, 8 F.3d 966, 971 (4th Cir. 1993) (asserting actual physical delivery of commodity is anticipated in cash forward contracts); *Commodity Futures Trading Comm'n v. Co Petro Mktg. Group, Inc.*, 680 F.2d 573, 578 (9th Cir. 1982) (stating that "a cash forward contract is one in which the parties contemplate physical transfer of the actual commodity"); *In re Stovall*, [1977-1980 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 20,941, at 23,778 (CFTC Dec. 6, 1979) (stating major distinguishing feature of cash forward contracts is legal obligation to deliver and generally fulfill expectation of delivery).

25. See MARKHAM, *supra* note 6, at 3 (describing development of to arrive contracts in response to various price and delivery-related problems in nineteenth century American grain markets). American grain markets suffered significant seasonal price variations due mainly to fluctuating supply. See *id.* Prices dropped dramatically as farmers flooded the market after the fall harvest. See *id.* Prices dropped so low that the cost of delivering crops to market became prohibitive. See *id.* As a result, much of the harvest would never be delivered and was wasted. See *id.* This led to shortages later in the year and associated dramatic price increases. See *id.* This cycle of supply and price shocks led buyers and sellers to seek means of securing prices and supplies in advance of actual delivery. See *id.* To arrive contracts provided a solution in which the parties agreed on the sale of a specific quantity and grade of grain at a set price to be delivered on a specific date in the future. See *id.*

William L. Stein provided a similar analysis in *The Exchange-Trading Requirement of the Commodity Exchange Act*, 41 VAND. L. REV. 473, 474-75 (1988). Stein, however, added the gloss that construction of storage helped alleviate the supply fluctuations, but did not solve the problems completely. See *id.* at 475. Forward contracts then developed in response to the problems of supply fluctuations, limited storage

both sides still retain some price and production risks, these risks are greatly reduced.²⁶

In contrast, parties to futures contracts are able to nullify their contractual obligations by executing offsetting transactions.²⁷ Thus, a holder

space and poor transportation. *See id.* When large dealers had insufficient supply to satisfy their commitments, they would enter forward contracts with grain producers. *See id.* The deferral of the delivery date resulted from the time delay in bringing the crops from the farm to the dealer. *See id.* Before long, parties recognized other significant benefits of forward contracts. *See id.* (asserting "sellers recognized . . . [their] utility . . . as a method of allowing for transportation time . . . [and] as a general method of merchandising" their crops). In addition, brokers could secure a source of supply without having to invest capital in storage facilities. *See id.* Ultimately, forward contracts led to greater efficiency in the markets, enabling "farmers to sell grain they expected to harvest and brokers to sell inventories they expected to acquire." *Id.*; *see* H.R. REP. NO. 93-975, at 130 (1974) ("A cash forward contract enables the buyer and the seller of commodities to properly plan for and utilize both storage and production facilities and to make commitments for deferred deliveries of the commodity or of further-processed products.").

Considering that grain farming and its inherent risks are as old as recorded history, it is not surprising that other observers trace the history of forward contracting as far back as ancient times. *See* KOLB, *supra* note 6, at 2-3 (asserting some authors trace history of forward contracting back to ancient Rome, classical Greece or even ancient India); MARKHAM, *supra* note 6, at 3 (citing various theories that date origins of futures trading back to Greco-Roman times or even as far as 2000 B.C., but noting that modern predecessor is to arrive contract developed in eighteenth century Europe).

26. *See* Iavarone, *supra* note 5, at 372-73 (explaining cash forward contracts do not eliminate all risk involved). For example, if a farmer enters a cash forward contract with an elevator to deliver 50,000 bushels of corn on December 1 at \$2.50 per bushel, the transaction reduces the farmer's price risk while increasing the production risk. *See id.* at 372. The farmer need not worry about the price dropping below \$2.50 per bushel, but the farmer will be liable to the elevator for breach of contract upon failure to deliver the full 50,000 bushels. *See id.* at 372-73. In addition to the lost income from the shortage, the farmer is likely to be liable for any special damages suffered by the elevator. *See id.* at 372.

For its part, the elevator assumes some of the farmer's price risk. *See id.* at 373. In this example, the elevator stands to lose if the market price drops significantly below the contract price. *See id.* Not only will the elevator be forced to acquire the grain at a higher price than it could have without the contract, but it will either have to sell it at a loss or incur storage costs in the hopes of being able to hold it until the price rises again. *See id.*

In a sense, the parties reduce their risks by trading them. *See* Solomon & Dicker, *supra* note 8, at 194 (stating forward contracts transferred price risk from grain producer to buyer). The farmer is willing to take on production risk in the form of a contractual obligation to deliver in return for a guaranteed price. *See id.* (noting farmers guaranteed delivery under forward contracts, but benefitted from securing specific price for crops). On the other hand, the elevator is better able to deal with falling prices than with uncertain supply, so it is willing to take on some price risk in return for the farmer's guaranty of delivery. *See id.* (noting grain buyers developed means of transferring price risk to speculators).

27. *See Noble Metals*, 67 F.3d at 772 (asserting party to futures contract can avoid delivery obligation by entering offsetting transaction); *Salomon Forex*, 8 F.3d at 971 (stating futures transactions seldom result in delivery because offsetting transactions extinguish obligation); *Cargill, Inc. v. Hardin*, 452 F.2d 1154, 1156-57 (8th Cir. 1971) (indicating that futures trader has choice between fulfilling deliv-

of a "short" position who has received payment for and is obligated to deliver a specific quantity of the commodity on a specific date can offset the obligation by taking a "long" position for the same quantity of the commodity.²⁸ Any interim price change in the futures contract will represent profit or loss on the transaction.²⁹ Offsetting transactions are made possible by standardization of futures contracts and highly liquid markets.³⁰ These factors free futures traders from some of the practical con-

ery obligation or offsetting and that 99% of futures transactions on Chicago Board of Trade are offset); *Stovall*, [1977-1980 Transfer Binder] Comm. Fut. L. Rep. (CCH) at 23,777 (asserting that "most parties to commodity futures contracts extinguish their legal obligation to make or take delivery by offsetting their contracts"); H.R. REP. NO. 93-975, at 130 (stating standardization of futures contracts meant parties could liquidate delivery obligation through offset); David J. Gilberg, *Regulation of New Financial Instruments Under the Federal Securities and Commodities Laws*, 39 VAND. L. REV. 1599, 1603 (1986) (asserting parties to futures contracts can extinguish delivery obligation through offset); Solomon & Dicker, *supra* note 8, at 197 (same); Mark D. Young & William L. Stein, *Swap Transactions Under the Commodity Exchange Act: Is Congressional Action Needed?*, 76 GEO. L.J. 1917, 1923-24 (1988) (same).

28. See *Cargill*, 452 F.2d at 1156-57 (describing typical futures transaction). A person who buys a commodity or has the right and obligation to take delivery of a commodity under a futures contract has what is called a "long" position. See *id.* (describing futures transactions); LEWIS H. BISBEE & JOHN C. SIMONDS, *THE BOARD OF TRADE AND THE PRODUCE EXCHANGE—THEIR HISTORY, METHODS AND LAW* 50 (1884) (defining long position); KOLB, *supra* note 6, at 2 (same); MARKHAM, *supra* note 6, at 203 (same). A person who sells a commodity or has the right and obligation to deliver the commodity under a futures contract, without actually possessing any of the commodity, has a "short" position. See *Cargill*, 452 F.2d at 1157 (defining "short" position); BISBEE & SIMONDS, *supra*, at 50 (same); KOLB, *supra* note 6, at 2 (same); MARKHAM, *supra* note 6, at 203 (same).

29. See *Co Petro*, 680 F.2d at 579-80 (describing settlement of futures contracts through offsetting transaction); KOLB, *supra* note 6, at 15-16 (same). Consider the following example: On June 1, trader A goes short one December corn contract at \$2.50 per bushel. In other words, A sells one contract to deliver 5000 bushels of corn in December and receives \$12,500 in return. See *id.* at 2 (describing short position). Because A is merely a futures trader and has no ability to produce or deliver the grain, A must offset the transaction to nullify the delivery obligation. See *id.* at 15 (describing offset). A does this by going long one December corn contract. See *id.* The December contract's equal and opposite obligation cancels out the delivery obligation of the short position. See *id.* at 15-17. If, in the interim, the price of corn for December delivery has dropped to \$2.00, for instance, A's profit is \$2500 (\$12,500 received for the short position less \$10,000 paid for the long position). See *id.* at 16. If the price has risen to \$3.00, however, A's loss is \$2500 (\$12,500 received for the short position less \$15,000 paid for the long position). See *id.*

30. See *Co Petro*, 680 F.2d at 579-80 (stating that "[t]he fungible nature of . . . [futures] contracts facilitates offsetting transactions"); H.R. REP. NO. 93-975, at 130 (stating development of interchangeability made offsetting transactions possible); MARKHAM, *supra* note 6, at 205 (stating standardization makes offsetting transactions possible, as trader wishing to offset long position can find trader who wishes to offset matching short position through clearinghouse); Committee on Commodities Regulation of the Ass'n of the Bar of the City of N.Y., *The Forward Contract Exclusion: An Analysis of Off-Exchange Commodity-Based Instruments*, 41 BUS. LAW. 853, 874 (1986) [hereinafter *Forward Contract Exclusion*] (stating fungibility of standardized contracts makes offsetting transactions possible).

straints that prevent parties to cash forward contracts from avoiding their obligations.³¹ The offsetting transaction is also what makes futures contracts speculative instruments as opposed to purely marketing instruments.³²

Courts and other observers have long recognized the important distinction between the use of contracts to protect against price changes and the use of contracts purely to speculate on price changes.³³ In Congress' efforts to curb speculation in the commodities markets, it has consistently exempted cash forward transactions from regulation.³⁴ Today, "contracts

31. See MARKHAM, *supra* note 6, at 203 (asserting cash forward contracts are "personalized," thus limiting their ability to be traded in secondary markets); Young & Stein, *supra* note 27, at 1924 (stating forward contracts, in contrast to futures contracts, are not fungible and are rarely offset).

32. See Gilberg, *supra* note 27, at 1603 (asserting primary purpose in trading futures is hedging price risks or speculating on price changes rather than purchasing or selling actual commodities); Solomon & Dicker, *supra* note 8, at 199 (describing principal participants in futures markets as hedgers, speculators and market makers). The primary difference between speculation and hedging is based on risk assumption. See *id.* at 199-200 (contrasting hedgers with speculators). Hedgers generally enter contracts to reduce risk associated with producing, buying and selling the underlying commodities. See *Board of Trade v. Christie Grain & Stock Co.*, 198 U.S. 236, 249 (1905) (defining hedging); KOLB, *supra* note 6, at 6 (describing hedgers); Solomon & Dicker, *supra* note 8, at 199 (same).

Speculators, by contrast, intentionally expose themselves to risk with the hope of profiting from price movements. See KOLB, *supra* note 6, at 147 (defining speculator as "a trader who enters the futures market in pursuit of profit, thereby accepting an increase in risk"); Solomon & Dicker, *supra* note 8, at 199-200 (describing speculators). Speculators have little or no involvement in trading the actual commodity. See *id.* at 200 (describing speculators); Young & Stein, *supra* note 27, at 1920 (same). Futures contracts developed as a means of transferring exposure from risk-averse hedgers to those more willing to speculate. See *Salomon Forex*, 8 F.3d at 971 ("The main purpose realized by entering into futures transactions is to transfer price risks from suppliers, processors and distributors (hedgers) to those more willing to take the risk (speculators)."); Stein, *supra* note 25, at 476 (discussing origins of futures contracts). The ability to enter offsetting transactions makes futures contracts attractive to speculators because it enables them to seek price-based profit opportunities without having to accept or make delivery of the underlying commodities. See H.R. Rep. No. 93-975, at 130 (noting offset capability led to increased use of futures contracts by speculators).

33. See *Board of Trade*, 198 U.S. at 249 (asserting contracts intended as hedges, even when settled other than by delivery, "stand on different ground from purchases made merely with the expectation that they will be satisfied by set-off"); *Embrey v. Jemison*, 131 U.S. 336, 344 (1889) (asserting contract for future delivery of goods is valid if actual delivery is intended, but "[i]f, under the guise of such contract, the real intent be merely to speculate in the rise or fall of prices . . . the whole transaction constitutes nothing more than a wager"); BISBEE & SIMONDS, *supra* note 28, at 287 (emphasizing distinction between gambling and legitimate speculation that is normal mercantile activity associated with commodity trading); Stein, *supra* note 25, at 477 (noting negative popular perception of speculators in early twentieth century at same time that Congress recognized legitimate, essential risk-shifting role of futures contracts in grain marketing).

34. See Glenn Willett Clark, *Genealogy and Genetics of "Contract of Sale of a Commodity for Future Delivery" in the Commodity Exchange Act*, 27 EMORY L.J. 1175, 1185 (1978) (tracing history of cash forward exclusion); *Forward Contract Exclusion*, *supra*

note 30, at 856-59 (same); Asklesen, *supra* note 5, at 129 (describing cash forward exclusion as feature of various laws regulating futures markets).

Congressional attempts to regulate futures trading date back to the 1840s. *See Forward Contract Exclusion*, *supra* note 30, at 856 (discussing history of futures regulation). State attempts date back to the 1860s. *See id.* In the nineteenth century, futures markets were plagued by rampant, often disastrous speculation. *See MARKHAM*, *supra* note 6, at 5-7 (describing notorious attempts to corner markets that led to collapses in wheat and gold markets). Price volatility in agricultural markets, which farmers blamed on the Chicago Board of Trade, led to increased congressional efforts in the late nineteenth and early twentieth centuries to rein in futures trading. *See id.* at 10 (discussing pressure on Congress from populist movement and Grangers to regulate futures trading and noting 200 such bills were introduced between 1880 and 1920).

The predecessor of modern futures regulation was the Cotton Futures Act of 1917, ch. 313, 39 Stat. 476 (1916). *See Clark*, *supra*, at 1183 (discussing early futures legislation). The Cotton Futures Act taxed contracts "of sale of any cotton for future delivery." Ch. 313, § 3, 39 Stat. 476. The Act made no distinction between cash forward and futures contracts. *See Clark*, *supra*, at 1183 (discussing Cotton Futures Act).

In 1921, Congress passed the Future Trading Act (FTA). Ch. 86, 42 Stat. 187 (1921). Congress' intent was to prevent price manipulation and what many perceived as excessive speculation in grains. *See Salomon Forex*, 8 F.3d at 970 (citing Stein, *supra* note 25, at 477 & n.23); *In re Stovall*, [1977-1980 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 20,941, at 23,779-80 (CFTC Dec. 6, 1979) (discussing legislative purposes of FTA). The FTA placed a tax on the sale of grain for future delivery. *See Forward Contract Exclusion*, *supra* note 30, at 857 (discussing FTA). The FTA excluded from the term "future delivery" "any sale of cash grain for deferred shipment or delivery." Ch. 86, § 2, 42 Stat. 187. The purpose of this exception (the cash forward exclusion) was to exempt legitimate forward transactions from the tax. *See Forward Contract Exclusion*, *supra* note 30, at 857 (discussing purpose of cash forward exclusion). Only one year after its inception, however, the Supreme Court struck down the FTA as an improper exercise of the taxing power. *See Hill v. Wallace*, 259 U.S. 44, 66 (1922) (finding "no ground upon which the provisions we have been considering can be sustained as a valid exercise of the taxing power").

Congress responded by passing the Grain Futures Act of 1922 (GFA), Pub. L. No. 67-331, ch. 369, 42 Stat. 998. *See Salomon Forex*, 8 F.3d at 970 (discussing GFA); *Forward Contract Exclusion*, *supra* note 30, at 857 (same); Stein, *supra* note 25, at 478 (same). The GFA served the same purposes as the FTA, but relied on Congress' power to regulate interstate commerce. *See Salomon Forex*, 8 F.3d at 970 (comparing GFA to FTA); *Forward Contract Exclusion*, *supra* note 30, at 857 (same); Stein, *supra* note 25, at 478 (same). The GFA prohibited "contract[s] of sale of grain for future delivery" except those executed on designated exchanges. Ch. 369, § 4, 42 Stat. 998, 999. This is commonly known as the "exchange trading requirement." *See Stein*, *supra* note 25, at 479 (discussing exchange trading requirement). The GFA retained the cash forward exclusion, permitting off-exchange contracts for the "sale of cash grain for deferred shipment or delivery." Ch. 369, § 2, 42 Stat. 998; *see Forward Contract Exclusion*, *supra* note 30, at 857 (stating GFA retained cash forward exclusion of FTA).

Collapses in the futures markets in the early 1930s created a perception that the GFA was too weak to serve its intended purposes. *See id.* at 858 (discussing history of GFA). In response, Congress amended the GFA in 1936, renaming it the Commodity Exchange Act (CEA) and extending the scope of federal regulation from grain to commodities in general. *See Commodity Exchange Act*, Pub. L. No. 74-675, ch. 545, 49 Stat. 1491 (1936); *Forward Contract Exclusion*, *supra* note 30, at 858 (discussing CEA). Again, the CEA retained the cash forward exclusion. *See Ch. 545, § 2, 49 Stat. 1491; Forward Contract Exclusion*, *supra* note 30, at 858 (discussing aspects of CEA). The latest major congressional action in regulating commodi-

of a sale of a commodity for future delivery" are subject to CFTC oversight under the CEA.³⁵ Under the CEA, it is illegal to sell such contracts except on CFTC designated exchanges.³⁶ The CEA, however, specifically excludes any "sale of cash Commodity for deferred shipment or delivery" from the term "future delivery."³⁷ The language is subtle, and the difference is often difficult to apply in any given case.³⁸ To make matters worse, the CEA does not provide legal definitions to distinguish between the terms.³⁹ As a result, courts have developed an operational distinction between the terms, focusing primarily on a fact-specific examination of whether the parties to a particular contract intended actual delivery of the commodity.⁴⁰

Much of the legal debate about HTAs focuses on whether they are cash forward contracts or futures contracts.⁴¹ Not surprisingly, judicial as-

ties was the creation of the Commodity Futures Trading Commission (CFTC) in 1974, in which Congress granted exclusive jurisdiction over contracts for future delivery of commodities. See Commodity Futures Trading Commission Act, Pub. L. No. 93-463, 88 Stat. 1389 (1974); *Forward Contract Exclusion*, *supra* note 30, at 859 (discussing creation of CFTC and noting cash forward exclusion has been retained).

35. Commodity Exchange Act, 7 U.S.C. §§ 1-25 (1994 & Supp. 1995) (granting CFTC jurisdiction over futures contracts).

36. See *id.* § 6(a).

37. *Id.* § 1a(11).

38. See *Salomon Forex*, 8 F.3d at 971 (describing difference as "semantically subtle"); *Commodity Futures Trading Comm'n v. Co Petro Mktg. Group, Inc.*, 680 F.2d 573, 577 (9th Cir. 1982) (describing statute as "ambiguous on its face").

39. See *Salomon Forex*, 8 F.3d at 971 (stating "futures contract" and "future" are not statutorily defined terms); *Co Petro*, 680 F.2d at 577 (stating "future delivery" and "cash commodity for deferred shipment or delivery" are not defined); *Oeltjenbrun v. CSA Investors, Inc.*, 3 F. Supp. 2d 1024, 1033-34 (N.D. Iowa 1998) ("['F]utures contracts' and 'cash forward contracts' are terms of art which do not appear in the [CEA].") (quoting *Commodity Futures Trading Comm'n v. Noble Metals Int'l, Inc.*, 67 F.3d 766, 772 n.4 (9th Cir. 1995)); *In re Grain Land Coop.*, 978 F. Supp. 1267, 1273 (D. Minn. 1997) (stating terms are not defined); Gilberg, *supra* note 27, at 1605 (stating neither CEA nor CFTC regulations define terms).

40. See *Noble Metals*, 67 F.3d at 772 (stating "exclusion is predicated on both parties contemplating and intending future delivery"); *In re Bybee*, 945 F.2d 309, 313 (9th Cir. 1991) (stating "the concept of delivery is the determining factor"); *Oeltjenbrun*, 3 F. Supp. 2d at 1036 ("[W]hether a contract contemplates actual delivery has been a recurring theme in judicial determinations of whether or not a contract memorializes a cash forward transaction."); *In re Stovall*, [1977-1980 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 20,941, at 23,778 (CFTC Dec. 6, 1979) (noting major difference between cash forward contracts and futures contracts is not only legal obligation to perform, but also "generally fulfilled expectation that the contract will lead to the exchange of commodities for money"); Gilberg, *supra* note 27, at 1605 (noting definition of terms has been left to CFTC and judicial interpretation, which has focused primarily on commercial nature of cash forward contracts and delivery obligation).

41. See *Johnson v. Land O'Lakes, Inc.*, 18 F. Supp. 2d 985, 988 (N.D. Iowa 1998) (stating issue of whether HTAs are cash forward or futures contracts is key issue in many cases); *Top of Iowa Coop. v. Schewe*, 6 F. Supp. 2d 843, 856 (N.D. Iowa 1998) (addressing question of whether HTAs are cash forward or futures contracts); *Oeltjenbrun*, 3 F. Supp. 2d at 1027 (same); see also Asklesen, *supra* note 5, at

assessment of the issue examines the parties' intent to deliver as evidence of whether they are truly a means of transferring title or are merely speculative devices.⁴² This determination is complicated because HTAs exhibit qualities of both cash forward and futures contracts.⁴³

B. HTAs and How They Work

Simple HTAs originated in the 1980s.⁴⁴ HTAs began as simple variants of cash forward contracts, but soon began to acquire more and more characteristics of futures contracts.⁴⁵ This process has progressed to the point that it is now possible to argue that newer versions of HTAs are more like speculative futures contracts than cash forward contracts.⁴⁶ Consider the following examples of simple HTAs and newer, more complex HTAs.

In a simple HTA, the buyer and seller base the eventual purchase price of the commodity on the futures contract price of the commodity for the same month that the seller anticipates actual delivery.⁴⁷ The eventual purchase price will be the futures contract price (set at the time the HTA is written) minus a "basis" equal to the difference between the futures contract price on the exchange and the local cash price for the commodity.⁴⁸ The basis tends to decrease, or "narrow," as the delivery date ap-

129 (stating that "question surrounding hedge-to-arrive contracts is whether they are future contracts . . . or whether . . . [they are] cash forward contracts").

42. See *Land O'Lakes*, 18 F. Supp. 2d at 994 (stating primary consideration is whether contracts contemplate actual physical delivery, measured by objective obligation and subjective intent); *Oeltjenbrun*, 3 F. Supp. 2d at 1037 (asserting contracts that create legal obligation to make or take delivery are outside scope of CEA); see also Iavarone, *supra* note 5, at 394 (observing issue is whether parties intended HTA "as a mechanism for transferring title or . . . engag[ing] in price speculation").

43. See Asklesen, *supra* note 5, at 123 (observing HTAs are combination of forward contract and short futures sale). For a further discussion of the features of HTA contracts, see *infra* notes 44-78 and accompanying text.

44. See Asklesen, *supra* note 5, at 123 (noting origins of HTAs).

45. See Iavarone, *supra* note 5, at 371-77 (comparing simple HTAs to newer, more complex versions with features similar to futures contracts). One commentator asserted that the development of more complex variants was a result of competition among aggressive grain merchants responding to the anticipated downfall of federal farm subsidy programs in the 1980s and the perceived need to extend price stability beyond the terms of cash forward contracts. See *id.* at 371-72 (describing evolution of complex HTAs).

46. See *id.* at 390 (asserting HTA is ineffective as hedging instrument and is useful only for speculation).

47. See *Eby v. Producers Co-op, Inc.*, 959 F. Supp. 428, 430 n.1 (W.D. Mich. 1997) (describing simple HTA contract); Iavarone, *supra* note 5, at 373 (same); Asklesen, *supra* note 5, at 124 (same).

48. See *Eby*, 959 F. Supp. at 430 n.1 (describing simple HTA and basis); Kolb, *supra* note 6, at 83 (defining basis); Iavarone, *supra* note 5, at 373 (describing simple HTA); Asklesen, *supra* note 5, at 124 (describing simple HTA and basis); Cole, *supra* note 5, at 250 (defining basis).

proaches.⁴⁹ Because the simple HTA allows the grain seller to set the basis at any time prior to the delivery date, it gives the seller the security of a relatively fixed price for the crops, plus the ability to play the market and take advantage of the narrowing basis.⁵⁰ For its part, the elevator will hedge against a price drop by taking a short position in the futures market corresponding to the quantity and delivery month of the HTA.⁵¹ Significantly, although slightly more speculative than pure cash forward contracts, simple HTAs do not alter in any way the parties' underlying delivery and receipt obligations.⁵²

In contrast, newer HTAs increase the level of speculation of simple HTAs by offering the farmer the ability to "roll" the delivery date into a different month.⁵³ Under these contracts, if the farmer elects to roll the

49. See KOLB, *supra* note 6, at 85-86 (demonstrating basis logically must diminish as delivery date approaches). Some factors that account for the difference between the local cash price and the futures price include transportation costs, changes in government policies, weather and storage availability. See Iavarone, *supra* note 5, at 373 n.7 (defining basis). Holding other components constant, the basis will reflect the transportation costs from the local market to the delivery site of the futures market. See *id.*

50. See Eby, 959 F. Supp. at 430 n.1 (describing simple HTA); Iavarone, *supra* note 5, at 374 (asserting simple HTA allowed farmers to speculate on basis); Cole, *supra* note 5, at 250 (describing benefits of HTAs).

51. See Eby, 959 F. Supp. at 430 (describing elevator's ability to hedge against price drop); Asklesen, *supra* note 5, at 124 (same). Assume, for example, that on May 1, the farmer and grain elevator enter into an HTA contract based on the farmer's expectation of delivering 5000 bushels of corn in December. At that time (May 1), the December futures price for corn is \$2.50 per bushel and the local cash price is \$1.75 per bushel. The basis, therefore, is \$.75 per bushel. The HTA sets a base price of \$2.50 per bushel (the current price of the December futures contract), but the final price for the farmer's corn will not be set until the farmer sets the basis, sometime before the delivery date. If on November 1, for instance, the December futures price has risen to \$2.75 per bushel and the local cash price has risen to \$2.25 per bushel, the basis has narrowed to \$.50. At this time, the farmer may wish to set the basis, securing a final selling price of \$2.00 per bushel (the \$2.50 December futures price agreed to on May 1, minus the \$.50 basis set on November 1). See generally Iavarone, *supra* note 5, at 373 (asserting basis tends to narrow as harvest approaches); Asklesen, *supra* note 5, at 124 (providing example of simple HTA in which elevator takes short position in futures market and farmer sets basis).

52. See Iavarone, *supra* note 5, at 374 (asserting simple HTA, from point of view of CEA, is virtually indistinguishable from cash forward contract).

53. See Johnson v. Land O'Lakes, Inc., 18 F. Supp. 2d 985, 997 (N.D. Iowa 1998) (recognizing HTAs permitted form of speculating); Barz v. Geneva Elevator Co., 12 F. Supp. 2d 943, 946 (N.D. Iowa 1998) (recognizing HTAs' rolling feature increases risk and allows producer to speculate); Oeltjenbrun v. CSA Investors, Inc., 3 F. Supp. 2d 1024, 1043 (N.D. Iowa 1998) (same); *In re Grain Land Coop.*, 978 F. Supp. 1267, 1276-77 (D. Minn. 1997) (conceding producers claimed rolling feature may have introduced inordinate risk); Countrymark Coop., Inc., v. Smith, No. 5-97-21, 1997 WL 762813, at *3 (Ohio Ct. App. Dec. 8, 1997) (acknowledging rolling feature increases risk and permits speculation); *Division of Economic Analysis Statement of Policy in Connection With the Unwinding of Certain Existing Contracts for the Delivery of Grain and Statement of Guidance Regarding Certain Contracting Practices*, 2 Comm. Fut. L. Rep. (CCH) ¶ 26,692, at 43,851 (1996) [hereinafter *CFTC Interpreta-*

HTA to a later month, the elevator will cover the short futures position (by purchasing a corresponding long position) and take a new short position corresponding to the new delivery month.⁵⁴ Although the elevator covers any margin requirements, it will deduct any losses on the futures transactions, along with administrative fees, from the farmer's eventual selling price.⁵⁵ For example, assume that a farmer and a grain elevator enter into

tive Statement] (concluding rolling can, in certain circumstances, create risk); Iavarone, *supra* note 5, at 376 (acknowledging rolling increases risk).

54. See *Grain Land Coop.*, 978 F. Supp. at 1269 (describing roll feature); *Eby*, 959 F. Supp. at 430 (same); *CFTC Interpretative Statement*, *supra* note 53, at 43,851 (same); Iavarone, *supra* note 5, at 375-76 (presenting example of how rolling works); Cole, *supra* note 5, at 249-50 (same).

55. See Iavarone, *supra* note 5, at 374 (describing benefits of HTAs); Asklesen, *supra* note 5, at 124-25 (describing fees and arrangements under HTAs); Cole, *supra* note 5, at 247 (asserting elevators commonly cover margin costs under HTAs). Margin is a good faith deposit of funds (usually cash or treasury securities) intended to ensure traders will fulfill contractual obligations. See KOLB, *supra* note 6, at 10 (defining margin). In addition to the initial margin deposit required to begin trading, there are also "maintenance" margins and "variation" margins. See *id.* at 11 (describing types of margins).

Any adverse price movements in the futures market will decrease the value of a trader's futures account. See *id.* (describing effect of price changes on margin). For every dollar by which a trader's account is reduced, a dollar is deducted from the trader's margin deposit. See *id.* Thus, if price changes reduce the value of a trader's futures account by \$150, that same amount is deducted from the account's margin. See *id.* (explaining margin). When the funds on deposit are reduced to a certain level (the maintenance margin, usually 75% of the initial margin), the trader faces a margin call. See *id.* (same). A margin call is a demand to deposit sufficient additional funds in the margin account to restore the account to its initial level. See *id.* (same). The amount of funds required to restore the margin account to its initial level is the variation margin. See *id.* (same).

Thus, an elevator engaged in an HTA with a farmer might experience the following events: Having contracted to purchase 5000 bushels of corn at the current December futures price of \$2.50 per bushel (less basis as set by the farmer), the elevator hedges against a price drop by selling short one December corn futures contract at \$2.50. See Asklesen, *supra* note 5, at 124 (describing simple HTA transaction). The value of this contract position is \$12,500 (5000 bushels at \$2.50 per bushel). A five percent initial margin would be \$625. If the futures price rises to \$2.52 per bushel, the value of the elevator's short position is reduced by \$100 (two cents per bushel times 5000 bushels), from \$1250 to \$1150. The \$100 reduction in the position will be deducted from the \$625 in the initial margin account, reducing it to \$525. If the December futures price drops down again, the increase in value will similarly be replaced in the margin account.

If at any time, however, the net cumulative effect of upward and downward movements causes the margin account to drop below its maintenance margin (75% of its initial margin level), the elevator will have to face a margin call. The elevator will then have to deposit variation margin sufficient to bring the margin account back up to its initial level (not just its maintenance level). Failure to do so will result in the account being closed. See generally KOLB, *supra* note 6, at 11-12 (giving example of margin funds flow in futures trading accounts as price of underlying commodity changes).

The additional problem with margin payments is that, once paid, they are not refundable until the price moves in the trader's favor and the value of the position increases. See Cole, *supra* note 5, at 253 (discussing margin calls). Thus, an elevator covering margin fees on a short position under an HTA risks accumulating

an HTA anticipating July delivery. If, prior to the delivery date, the price of the July futures contract drops while the December contract price remains relatively high, the farmer may be able to benefit by rolling forward into the December contract.⁵⁶ In this situation, the farmer can take a profit on closing out the short July futures position and still secure a high base price for the sale of the underlying grain.⁵⁷ Conversely, the farmer may also benefit from a backwards roll (from a December futures contract into a September futures contract, for instance) if futures prices move in the other direction.⁵⁸

The roll capability introduces three possible dangers.⁵⁹ First, it creates the temptation for a farmer to turn the HTA into a pure short futures position by selling the crop on the cash market and rolling the HTA forward to defer the delivery obligation until after the next harvest.⁶⁰ By itself, such a situation is not particularly dangerous for either the farmer or the elevator, which makes its own commitments in reliance on the farmer's promise to deliver, as long as the farmer maintains the ability to meet delivery obligations for crops committed under the HTA.⁶¹ Never-

margin costs until the farmer delivers the grain and enables the elevator to close out the futures position. *See id.*

A similar problem with HTAs involves arranging the profits and losses on the futures transactions associated with rolling. *See Asklesen, supra* note 5, at 126-27 (describing effects of rolling HTAs); Cole, *supra* note 5, at 250 (same). If the farmer chooses to roll the HTA under conditions that incur a loss on the transaction, the elevator will pass the loss through to the farmer only when the contract is fulfilled. *See Asklesen, supra* note 5, at 126-27 (describing elevators' losses from producers' decisions to roll). In the meantime, the elevator bears the financial burden of carrying accumulated futures losses as well as accumulated margin costs until the farmer delivers the grain. *See id.* at 126 (noting elevators bear losses on futures transactions until farmer delivers grain and closes out HTA).

56. *See generally* Cole, *supra* note 5, at 249-50 (providing example of rolling transaction under HTA in which farmer sells underlying commodity on cash market). By way of illustration, assume that at the time the parties enter into the HTA, the July futures price is \$2.25 and the December price is \$2.65. If the price of the July futures contract drops to \$2.00 and the December futures contract price drops to \$2.50, the roll will yield a \$.25 per bushel profit for the farmer (less administrative fees) on the futures transaction (\$2.25 minus \$2.00) and still enable the farmer to secure a \$2.50 base price (the December futures price at the time of the roll).

57. *See id.* (describing rolling HTA).

58. *See id.* (providing example of rolling HTA).

59. For a discussion of the additional risks associated with rolling HTAs, see *infra* notes 59-73 and accompanying text.

60. *See* Cole, *supra* note 5, at 250 (describing hypothetical operation of HTA); *see also CFTC Interpretative Statement, supra* note 53, at 43,851 (explaining HTA contracts expose farmer to risk of futures losses when farmer cannot deliver grain).

61. *See CFTC Interpretative Statement, supra* note 53, at 43,851 (explaining risks involved with short position when farmer is unable to deliver grain). Compared to long positions, whose value can drop only to zero, pure short positions always carry unlimited risk in that the position holder is obligated to buy back the underlying commodity or a corresponding long position whose value has no upper limit. *See Iavarone, supra* note 5, at 378 n.32 (describing risk of short futures position).

theless, elevators holding the short positions for the farmers are subject to margin calls when futures prices rise and thus face a great deal of risk when the farmer has no grain to deliver.⁶²

The second danger is that rolling can expose farmers to the negative market dynamics of multiple crop years.⁶³ A crop year is the twelve-month period beginning when newly harvested grain is available and ending when the next crop's harvest becomes available.⁶⁴ The crop year for corn futures begins with the fall harvest and includes December, March, May and July contracts with September as a transition month at the end of the old crop year and the beginning of the new crop year.⁶⁵ The danger lies in the fact that different crop years for seasonal commodities are subject to different market dynamics, and as a result, the farmer bears separate risks in the cash market and the futures market.⁶⁶ When the parties use this crop year's futures contract to establish the price of next year's corn, the anticipated crop is subject to the market forces determining the price of the next (new) crop year, while the elevator's short position (whose profits or losses are passed on to the farmer) is subject to the market forces determining the price of the current (old) crop year.⁶⁷ Thus, the farmer can lose on both parts of the transaction.⁶⁸

62. See Cole, *supra* note 5, at 252 (describing financial strain on elevators from margin calls on short futures positions that neither elevators nor farmers could close out, in part because farmers had sold their crop on cash market).

63. See *CFTC Interpretative Statement*, *supra* note 53, at 43,850-51 (explaining futures prices for different crop years can move independently of each other and futures month chosen for purposes of setting HTA price may be in different crop year than anticipated harvest); Iavarone, *supra* note 5, at 376-78 (asserting rolling forces farmer to become exposed to different price dynamics of separate crop years).

64. See *CFTC Interpretative Statement*, *supra* note 53, at 43,849 (defining crop year).

65. See Iavarone, *supra* note 5, at 376 n.23 (describing crop year for corn).

66. See *id.* at 376-77 (describing increased risks of exposure to price dynamics of different crop years).

67. See *id.* (discussing negative effects of establishing delivery price of grain from new crop year on futures contract price of old crop year).

68. See *id.* (discussing possible result of new crop/old crop spread). A farmer who uses an old crop year futures contract to price a new crop year harvest technically has what is known as a spread in the futures market. See *id.* (describing "bear spread"). That is, the farmer has a long position in new crop corn futures and a short position in old crop corn futures. See *id.* This hedge works for the farmer when both "legs" tend to move in sympathy. See *id.* (discussing effect of spread position). Thus, any drop in the cash price for the farmer's old crop corn (a loss in the long position) is usually offset by a similar drop in the futures price of the new crop corn (resulting in a profit in the short position). See *id.* (same). Nevertheless, old crop corn and new crop corn are subject to different market forces, and both legs of the spread can move in opposite directions, resulting in a loss in both positions. See *id.* (discussing effect of spread position when legs of spread move independently of each other).

The third danger arises because rolling enables farmers to make multiple futures transactions based on one contract for the sale of grain.⁶⁹ As a result, the farmer can accumulate futures losses that far outweigh any offsetting profits from the sale of the underlying commodity, and the only limit on those losses is the eventual obligation to deliver the grain and close out the HTA.⁷⁰ Some argue, however, that rolling effectively eliminates the ultimate obligation by allowing farmers to put off delivery indefinitely.⁷¹ Thus, the farmer has greater risk of incurring futures losses, and the elevator's financial resources are placed in greater jeopardy.⁷² This situation increases exposure to margin calls and decreases cash flow because the elevator is forced to absorb and carry losses on the futures transactions until the farmer eventually delivers on the HTA.⁷³

Some recognized these inherent dangers and attempted to warn of the risks of irresponsible HTA dealings.⁷⁴ Unfortunately, many failed to heed the warnings and suffered tremendous losses as drastic price increases in 1995 and 1996 exposed those risks.⁷⁵ Throughout 1995 and 1996, elevators felt the increasing financial pressure of carrying farmers' accumulated futures losses resulting from liberal rolling of HTA contracts in previous years and repeated margin calls on their open short positions

69. See *Oeltjenbrun v. CSA Investors, Inc.*, 3 F. Supp. 2d 1024, 1043 (N.D. Iowa 1998) (acknowledging rolling may result in futures transactions without parallel transactions in underlying grain).

70. See Cole, *supra* note 5, at 251-52 (noting farmers' losses grew with each roll in 1996). Farmers who stood to incur losses due to price increases in 1996 rolled their HTAs rather than deliver and take the loss. See *id.* (discussing events of 1996). As prices continued to rise, however, the farmers stood to lose even more if they closed out their HTAs. See *id.* Thus, farmers found themselves in the position of having to keep rolling in the hopes that prices would come down and enable them to close out their HTAs without incurring even greater losses. See *id.*

71. See *Oeltjenbrun*, 3 F. Supp. 2d at 1043 (stating *Oeltjenbrun* argued that allowing unlimited rolling nullified delivery requirement); *In re Grain Land Coop.*, 978 F. Supp. 1267, 1277 (D. Minn. 1997) (addressing producers' argument that rolling eliminates delivery requirement); see also Iavarone, *supra* note 5, at 400 (asserting farmer is not required to deliver under flex HTA).

72. See *Grain Land Coop.*, 978 F. Supp. at 1270 (noting costs associated with rolling put elevator in difficult financial position); see also Asklesen, *supra* note 5, at 126 (explaining elevators bear costs of rolling until producer delivers grain and closes out HTA); Cole, *supra* note 5, at 252 (observing elevators face bankruptcy if unable to cover futures positions due to farmers' failure to deliver grain). For a further discussion of futures-related financial strains on elevators, see *supra* note 55 and accompanying text.

73. See Asklesen, *supra* note 5, at 126-27 (noting strain on elevators of bearing futures losses and "enormous" margin calls); Cole, *supra* note 5, at 252-53 (discussing burden of margin calls on elevators).

74. See *CFTC Interpretative Statement*, *supra* note 53, at 43,851-52 (identifying "prudent" and "imprudent" risk-reduction activities); Iavarone, *supra* note 5, at 378 n.35, 388 n.68 (noting warnings issued by National Grain & Feed Association).

75. See Asklesen, *supra* note 5, at 127-28 (discussing severe economic losses suffered in 1996 from HTAs); Cole, *supra* note 5, at 243-44 (providing individual examples of HTA-related losses).

triggered by the rising grain prices.⁷⁶ Threatened with financial ruin, elevators sought to force farmers to deliver grain committed under HTAs and close out their futures positions, only to find that many farmers had sold that year's crop, had HTA commitments far in excess of what they could possibly deliver or both.⁷⁷ The inability of both sides to withstand further losses under these contracts led to the current outbreak of litigation.⁷⁸

C. *Judicial Interpretation of the Cash Forward Exclusion*

The CEA provides no guidance for understanding the distinction between "contracts for future delivery" and "sales of cash commodities for deferred shipment or delivery."⁷⁹ As a result, courts have developed their own understanding of the cash forward exception through case law.⁸⁰

In *In re Stovall*,⁸¹ the first major case dealing with the cash forward exclusion, the court identified six features of a futures contract falling within the regulatory reach of the CEA.⁸² That court observed that all six

76. See *Grain Land Coop.*, 978 F. Supp. at 1270 (noting Grain Land's financial difficulties from costs associated with rolling); see also Asklesen, *supra* note 5, at 127-28 (noting strain on elevators from margin calls).

77. See *Johnson v. Land O'Lakes, Inc.*, 18 F. Supp. 2d 985, 992 (N.D. Iowa 1998) (noting farmers' commitments under HTAs exceeded annual production and farmers sold corn on cash market then rolled their HTAs); *Grain Land Coop.*, 978 F. Supp. at 1270 (describing Grain Land's attempts to enforce farmers' delivery obligations); see also Asklesen, *supra* note 5, at 127-28 (discussing lawsuits triggered by elevators' attempts to force farmers to deliver grain); Cole, *supra* note 5, at 252 (discussing pressures on elevators that forced them to make demands on farmers). In many cases, the farmers could not deliver because they had either committed more grain to HTA contracts than they could produce or sold their grain on the cash market and rolled their contracts intending to deliver on them in the next crop year. See *id.* (discussing lack of grain to fulfill HTA obligations).

78. See Asklesen, *supra* note 5, at 127 (noting number of lawsuits resulting from developments of 1995 and 1996); Cole, *supra* note 5, at 252 (describing elevators' demands on farmers).

79. For a further discussion regarding this distinction, see *supra* notes 38-40 and accompanying text.

80. See Gilberg, *supra* note 27, at 1605 (stating definition has been left to CFTC and courts).

81. [1977-1980 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 20,941, at 23,777 (CFTC Dec. 6, 1979).

82. See *id.* (describing commodity futures transactions). Stovall was charged with soliciting and accepting orders for illegal futures contracts. See *id.* at 23,776. The Administrative Law Judge ("ALJ") found that Stovall directed his business primarily at the general public as opposed to customers interested in trading the actual underlying commodities. See *id.* at 23,778. Because only one customer ever took delivery, which represented a small portion of the customer's transactions (and an even smaller portion of Stovall's), the court found that the contracts were never intended to transfer ownership of the commodities. See *id.* (noting few of Stovall's transactions were motivated by desire to trade actual commodities). The ALJ also found that Stovall promoted the contracts for speculative purposes. See *id.* (asserting Stovall's transactions were used and promoted as means of speculation).

In addition, Stovall's contracts were standardized like futures contracts traded on registered exchanges. See *id.* at 23,778-79. Once the customer chose a delivery month, a program determined the exact delivery date, location, contract size and

features need not be present.⁸³ According to the court, futures contracts are: 1) standardized contracts for the purchase or sale of a commodity; 2) for future, as opposed to immediate delivery; 3) directly or indirectly offered to the general public; and 4) generally secured by earnest money, or "margin."⁸⁴ Fifth, the purpose of a futures contract is to shift risk rather than to transfer ownership.⁸⁵ Sixth and finally, although the parties may eventually perform on the contract, the ability to offset effectively removes the delivery obligation.⁸⁶ The court contrasted these characteristics with cash forward contracts in which the parties expected actual delivery of the commodity and in which "[t]he seller would necessarily have the ability to deliver and the buyer would have the ability to accept delivery in fulfillment of the contract."⁸⁷

A few years later, the United States Court of Appeals for the Ninth Circuit addressed the distinction between cash forward and futures contracts in *Commodity Futures Trading Commission v. Co Petro Marketing Group, Inc.*⁸⁸ The court found the distinction was initially drawn to "meet a particular need such as that of a farmer to sell part of next season's harvest at a set price."⁸⁹ The court described a party to a cash forward contract as one for whom the commodity has "inherent value," as evidenced by the ability to make or take delivery of the commodity.⁹⁰ The court also noted that while standardization is an important feature of futures contracts, the rigid uniformity of contracts traded on licensed exchanges is not necessary.⁹¹ Rather, the ability to nullify the delivery obligation through offset-

handling fees. *See id.* Most importantly, almost every contract was offset by an equal and opposite contract between Stovall and the customer, with a cash transaction settling any gain or loss. *See id.* As the court noted, "this lack of delivery is the clearest indication that the contracts were not cash commodity contracts for deferred shipment or delivery." *Id.* at 27,779.

83. *See id.* (asserting futures contracts need not include all elements mentioned).

84. *See id.* at 23,777 (describing common features of futures contracts).

85. *See id.* (discussing primary purpose of futures contracts).

86. *See id.* (noting common use of offsetting transactions to extinguish delivery obligations in futures contracts).

87. *Id.* The court noted that the major difference between "excluded cash commodity-deferred delivery" contracts and futures contracts is that delivery is a "generally fulfilled expectation" of excluded contracts, but is rarely fulfilled in futures contracts. *Id.* at 27,778.

88. 680 F.2d 573 (9th Cir. 1982). Co Petro sold contracts to the general public for future delivery of petroleum products. *See id.* at 576. Under these "Agency Agreements," the customer would appoint Co Petro as agent to purchase a specific quantity and type of fuel at a fixed price to be delivered at an agreed upon date. *See id.* The customer then paid a deposit and could later take delivery, appoint Co Petro to sell the fuel or cancel the contract and pay liquidated damages provided for in the contract. *See id.* at 577, 580.

89. *Id.* at 577.

90. *See id.* at 578 (describing buyer in cash forward contract).

91. *See id.* at 580-81 (admitting contracts were not as standardized as those traded on licensed exchanges, but nonetheless were sufficiently uniform to constitute futures contracts). The Agency Agreements were traded in multiples of uni-

ting contracts is essential.⁹² Other means of nullifying, such as canceling the contract and paying liquidated damages, can also be characteristic of a futures contract.⁹³

The Ninth Circuit again dealt with the cash forward exclusion in *In re Bybee*.⁹⁴ In that case, the court interpreted its previous ruling in *Co Petro* as requiring subjective intent to deliver and an objective showing of a delivery obligation.⁹⁵ The court also took note of CFTC releases recognizing that parties who contemplate delivery and are capable of making or taking delivery may nevertheless settle instead by cash payment.⁹⁶ Such "book-out" agreements, however, are usually characterized by the following: 1) they are separately negotiated; 2) they are not provided for in the terms of the contract; and 3) any party in the chain of distribution may still require delivery.⁹⁷ Thus, in recognition of economic realities, the court held that the cash forward exception could still apply in some cases even when the parties nullify the delivery obligation.⁹⁸

form basic units of volume, prices were set unilaterally at then-prevailing market rates and important dates for delivery and notification were mostly uniform. *See id.* Considering this degree of standardization, the court found the Agency Agreements offset and cancellation provisions enabled customers to trade in futures free of delivery obligations. *See id.* at 580 (noting purpose of standardization in futures contracts is to facilitate offsetting and recognizing *Co Petro* was obliged to execute such transactions).

92. *See id.* (noting standardization of futures contracts is important to facilitate offsetting transactions).

93. *See id.* (treating liquidation as means of canceling delivery obligation in Agency Agreements).

94. 945 F.2d 309 (9th Cir. 1991). Bybee purchased precious metals from a supplier under a "Deferred Delivery" plan and resold them to retail customers. *See id.* at 310-11. Bybee made a down payment and the supplier secured the balance due with a lien on all undelivered metals. *See id.* Final delivery was scheduled to take place upon final payment of the full balance. *See id.* Even though the contracts were not completely standardized, the court determined they were futures contracts because the supplier was willing to offset them. *See id.* at 313 (holding transactions were futures contracts because of implicit provision for offset). Nonetheless, the court determined that they satisfied the cash forward exception because each party could still enforce the other party's legal obligation to make or take delivery. *See id.* at 315 (holding exchange trading requirement inapplicable because parties retained delivery obligations).

95. *See id.* at 313 (describing holding in *Co Petro*).

96. *See* Statutory Interpretation Concerning Forward Transactions, 55 Fed. Reg. 39,188, 39,191 (1990) [hereinafter *Statutory Interpretation*] (observing contracts between commercial parties may serve same functions as valid cash forward contracts, notwithstanding ultimate settlement in form of cash payment); Regulation of Hybrid and Related Instruments, 52 Fed. Reg. 47,022, 47,027 (1987) [hereinafter *Regulation of Hybrid Instruments*] (recognizing contracts in which parties are capable of fulfilling delivery obligations may occasionally be settled without delivery pursuant to privately negotiated agreements between principals).

97. *See Bybee*, 945 F.2d at 314 (providing description of "bookout" agreements). A "bookout" agreement offsets the contractual delivery obligation with newly agreed upon consideration (usually cash). *See id.*

98. *See id.* at 315 (concluding cash forward exception applied to Deferred Delivery contracts). The *Statutory Interpretation* noted that regulation of futures con-

The Ninth Circuit examined cash forward and futures contracts yet again in *Commodity Futures Trading Commission v. Noble Metals International, Inc.*⁹⁹ The court acknowledged the previously recognized reality that the mere appearance of a delivery obligation would not suffice to bring contracts within the cash forward exception.¹⁰⁰ By their terms, the contracts may indicate a binding delivery obligation and satisfy the cash forward exclusion, but the courts may place greater emphasis on the parties' actual conduct under the contracts.¹⁰¹

The United States District Court for the Northern District of Iowa first addressed the possible application of the cash forward exclusion to HTAs in *Oeltjenbrun v. CSA Investors, Inc.*¹⁰² In *Oeltjenbrun*, the court determined that the HTAs in question were valid cash forward contracts, primarily based on evidence that the contracts contemplated actual delivery of the commodity because the parties were engaged in the business of producing and trading grain, the parties were capable of making and taking delivery and the commodity had "inherent value" to them.¹⁰³ Additionally, the court concluded that because the contracts contained no specific provi-

tracts should not extend to commercial contracts with enforceable delivery obligations "in which delivery is deferred for commercial convenience and necessity." Statutory Interpretation, *supra* note 96, at 39,190.

99. 67 F.3d 766 (9th Cir. 1995). Under the defendants' "Forward Delivery Program," a customer, drawn from the general public, purchased the right and obligation to receive specified quantities of precious metals at an agreed-on price. *See id.* at 769. The customer paid a 15% "administrative fee." *See id.* Upon payment of the contract price, the customer received title to the metals. *See id.* The contracts stipulated that performance of the delivery obligation was mandatory and that offsetting transactions were prohibited. *See id.* Despite these provisions, the defendants arranged for customers to liquidate their positions through a third party who would sell the metals back to the defendants. *See id.*

100. *See id.* at 773 (finding parties had no legitimate expectation of delivery, and thus contracts were subject to CEA despite superficial obligation to perform and prohibition on offsetting transactions); *Commodity Futures Trading Comm'n v. American Metal Exch. Corp.*, 693 F. Supp. 168, 192 (D.N.J. 1988) (finding investment program in which delivery rarely occurred and could be avoided through offset or liquidation involved futures contracts despite superficial requirement of actual delivery); *Commodity Futures Trading Comm'n v. Morgan, Harris & Scott, Ltd.*, 484 F. Supp. 669, 676 (S.D.N.Y. 1979) (asserting that "self-serving labels that [parties] choose to give their contracts should not deter the conclusion that their contracts are [futures contracts]").

101. *See Noble Metals*, 67 F.3d at 772-73 (rejecting argument that paper transfer of title satisfied delivery obligation); *Commodity Futures Trading Comm'n v. Co Petro Mktg. Group, Inc.*, 680 F.2d 573, 581 (9th Cir. 1982) ("The transaction must be viewed as a whole with a critical eye toward its underlying purpose.").

102. 3 F. Supp. 2d 1024 (N.D. Iowa 1998). In 1995, Bradley Oeltjenbrun, a grain farmer in central Iowa, committed 120,000 bushels of corn to HTA contracts with three different grain elevators. *See id.* at 1028-29 (reviewing contracts between parties). The specificity of the delivery obligations varied with each elevator. *See id.* at 1039-45 (describing contracts' provisions in detail). Oeltjenbrun rolled each HTA at least once, but only delivered some of the grain under the contracts. *See id.* at 1029-30 (discussing parties' performance under contracts).

103. *See id.* at 1039-40, 1042, 1044-46 (discussing evidence of delivery obligation in each contract).

sions regarding rolling, the rolls executed were similar to the separate, individually negotiated bookout agreements in *Bybee*.¹⁰⁴ Shortly thereafter, the same court faced some of the same issues in *Top of Iowa*.¹⁰⁵

III. THE FACTS OF *TOP OF IOWA COOPERATIVE V. SCHEWE*

In the spring and summer of 1995, Virgil E. Schewe, a farmer in Freeborn County, Minnesota, entered into five contracts with Top of Iowa Cooperative.¹⁰⁶ All five contracts were of the same standardized form and had individual entries filled in by hand.¹⁰⁷ Each contract acknowledged that Top of Iowa had taken, on Schewe's behalf, a short position on the Chicago Board of Trade.¹⁰⁸ The individual entries, filled in separately for each of the contracts, detailed the commodity (corn), the quantity, the futures delivery month (month in which Schewe anticipated delivering the grain) and the current futures price for that delivery month.¹⁰⁹ Beyond a statement that "[t]his is NOT considered a credit sale contract as long as final price is determined before delivery," the contracts did not directly reference any obligation to deliver grain to the elevator.¹¹⁰ The contracts also contained no specific provision allowing Schewe to roll the contract into any other month.¹¹¹

Schewe attempted to deliver his grain in the fall of 1995, but could not do so because the elevator was full.¹¹² Schewe then rolled the contracts into the spring of 1996 and the HTAs were repriced accordingly.¹¹³ Schewe canceled the contracts on May 31, 1996, asserting that Top of Iowa had breached by changing the terms of the roll.¹¹⁴ Schewe never delivered any grain on the contracts.¹¹⁵

104. *See id.* at 1043-44, 1047 (comparing rolling of HTAs to bookout agreements and determining that rolling has even smaller effect on delivery obligation than bookouts).

105. *See Top of Iowa Coop. v. Schewe*, 6 F. Supp. 2d 843 (N.D. Iowa 1998).

106. *See id.* at 847 (describing nature of relationship between parties).

107. *See id.* at 847-48 (describing HTA contracts between Schewe and Top of Iowa).

108. *See id.*

109. *See id.* at 848.

110. *Id.* at 854 (quoting Complaint ¶ 9, *Top of Iowa*, 6 F. Supp. 2d at 843 (No. C 96-3146-MWB)). The HTAs make reference, however, to an attached "Grain Purchase Contract and Confirmation" that may have included more specific delivery information, but neither party provided a copy of it. *See id.* at 848. The manager of one of the grain elevators in *Oeltjenbrun* asserted that the Grain Purchase Contract and Confirmation was never attached until the seller established the final sales price by setting the basis. *See Oeltjenbrun v. CSA Investors, Inc.*, 3 F. Supp. 2d 1024, 1046 (N.D. Iowa 1998).

111. *See Top of Iowa*, 6 F. Supp. 2d at 848 (noting contract did not specifically provide for rolling).

112. *See id.* (adding neither party disputed elevator was full).

113. *See id.* (noting factual dispute regarding which party requested rolling HTAs).

114. *See id.* at 848-49 (explaining why Schewe canceled contracts).

115. *See id.* (noting that no grain was ever delivered on any contracts).

At trial, both parties filed motions for summary judgment on the issue of whether the HTAs were illegal off-exchange futures contracts or whether they came within the cash forward exclusion.¹¹⁶

IV. ANALYSIS

A. Narrative Analysis

The court began its analysis of the issue by citing the proposition that “self-serving labels . . . should not deter the court” from determining whether particular contracts are futures contracts.¹¹⁷ The court then acknowledged the Ninth Circuit’s observation in *Co Petro* that “‘no bright-line definition or list of characterizing elements is determinative’” of whether a contract is a cash forward contract or a futures contract and that “[t]he transaction must be viewed as a whole with a critical eye toward its underlying purpose.”¹¹⁸

Next, the court cited its previous decision in *Oeltjenbrun*, recalling that the issue in cases dealing with the cash forward exclusion was whether there was any obligation to deliver.¹¹⁹ As in *Oeltjenbrun*, the court found that the obligation to deliver in the present case was, at best, implied.¹²⁰ The obligation in *Top of Iowa* was only an inference based on the details of the futures transaction and an oblique reference to delivery in the last paragraph of the contract.¹²¹ The court noted, however, that Schewe had repeatedly asserted his intent to deliver grain under the contract.¹²² The

116. *See id.* at 847.

117. *Id.* at 853 (citing *Commodity Futures Trading Comm’n v. Noble Metals Int’l, Inc.*, 67 F.3d 766, 773 (9th Cir. 1995)).

118. *Id.* (quoting *Commodity Futures Trading Comm’n v. Co Petro Mktg. Group, Inc.*, 680 F.2d 573, 581 (9th Cir. 1982)).

119. *See id.* at 854 (reviewing *Oeltjenbrun* decision); *see also In re Bybee*, 945 F.2d 309, 313 (9th Cir. 1991) (noting cash forward exclusion was intended to apply only to contracts in which parties expect delivery of actual commodity); *Co Petro*, 680 F.2d at 578 (emphasizing fact that parties to cash forward contracts deal in and contemplate delivery of actual commodity).

120. *See Top of Iowa*, 6 F. Supp. 2d at 854 (finding only implied obligation to deliver); *Oeltjenbrun v. CSA Investors, Inc.*, 3 F. Supp. 2d 1024, 1046 (N.D. Iowa 1998) (observing *Oeltjenbrun*’s obligation to deliver under HTAs as “an inference” arising from contract’s terms “that the transaction concerns a specified quantity of grain of a specified condition with a specified ‘Arrival Period,’ ‘Destination,’ and ‘Futures Option Price’”).

121. *See Top of Iowa*, 6 F. Supp. 2d at 854 (describing indirect references to delivery obligation under HTAs).

122. *See id.* at 855 (believing Schewe “stated repeatedly that his intention was to make actual physical delivery”). The court relied on Schewe’s statements of subjective intent to establish the existence of a binding delivery obligation in much the same way that other courts have looked to the parties’ course of performance to determine the lack of a delivery obligation. *See id.* (“[T]he parties’ intention that delivery occur clarifies any uncertainty as to an actual delivery obligation under the ambiguous terms of the HTAs.”); *Noble Metals*, 67 F.3d at 772-73 (determining that defendants had no legitimate expectation that customers would take delivery based on fact that very few of “vast number of purchasers . . . contem-

court went on to explain that the HTAs here were between parties who were engaged in the business of producing, buying and selling grain and were capable of making and taking delivery of the commodity.¹²³ The grain contracts thus had inherent value to the parties by providing for the sale of some of the farmer's crop and providing the elevator with a source of supply for its business.¹²⁴

Because the HTAs in the present case contained no express provision either permitting or forbidding rolling, the court held that, at most, the elevator voluntarily permitted it.¹²⁵ Because the elevator executed the rolls voluntarily, the court found rolling in this instance analogous to the bookout agreements discussed in *Bybee* (i.e., individually negotiated and separate from the HTAs themselves).¹²⁶ Significantly, although Top of Iowa permitted rolls in administering the HTAs, it was not legally obliged to do so.¹²⁷ As a result, the court reasoned that the rolls did not negate the delivery requirement.¹²⁸

plated actual delivery"); *Co Petro*, 680 F.2d at 580 (determining customers' ability to offset or liquidate positions eliminated delivery obligation).

In this area of law, it is well recognized that the wording of the contracts is rarely a credible indication of actual intent. See *Noble Metals*, 67 F.3d at 773 (rejecting reliance on "self-serving labels") (citing *Commodity Futures Trading Comm'n v. American Metal Exch. Corp.*, 693 F. Supp. 168, 192 (D.N.J. 1988)); *Melchert v. American Union Tel. Co.*, 11 F. 193, 196 (D. Iowa 1882) (acknowledging parties to illegal futures contracts "will always seek to give them the form and semblance of legality"). Nevertheless, it is equally well recognized that some parties to futures contracts occasionally deliver the actual commodity. See *In re Stovall*, [1977-1980 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 20,941, at 23,777 (CFTC Dec. 6, 1979) ("[A] party to a commodity futures contract may eventually perform on the contract . . ."); H.R. REP. NO. 93-975, at 129 (1974) (asserting less than three percent of futures contracts are settled by delivery); KOLB, *supra* note 6, at 15 (discussing delivery as means of settling futures contract, but noting that "in the fiscal year ending September 30, 1989, only about one-half of one percent of all contracts traded were settled by either physical delivery or cash settlement") (citing COMMODITY FUTURES TRADING COMMISSION ANNUAL REPORT 101 (1989)). Thus, Schewe's intent to deliver may establish that the HTAs were valid cash forward contracts only in his case. See *Top of Iowa*, 6 F. Supp. 2d at 846 (asserting court must examine each case individually). It is still possible that Top of Iowa generally contemplated HTAs with other parties as off-exchange futures transactions. See Iavarone, *supra* note 5, at 396 (arguing determination of validity of elevator's HTAs should include examination of elevator's dealings with all customers).

123. See *Top of Iowa*, 6 F. Supp. 2d at 855 (discussing evidence that actual delivery was purpose of contracts).

124. See *id.* (discussing principal purpose of contracts).

125. See *id.* at 856 (determining that rolling did not negate delivery obligation while indicating HTAs in question were futures contracts because both parties retained right to demand performance).

126. See *id.* (analogizing this case with previous Ninth Circuit case); see also *In re Bybee*, 945 F.2d 309, 314 (9th Cir. 1991) (describing bookout agreements).

127. See *Top of Iowa*, 6 F. Supp. 2d at 856 (discussing decision to roll HTAs). For a discussion of market pressures that may effectively oblige elevators to roll at the customers' insistence, see *infra* note 155 and accompanying text.

128. See *Top of Iowa*, 6 F. Supp. 2d at 856 (holding that delivery obligation still existed).

Schewe asserted that the court in *Oeltjenbrun* found that the HTAs in question were valid cash forward contracts merely because the parties involved were a farmer and a grain elevator.¹²⁹ Such reasoning, he claimed, excluded farmers from regulatory protection against commodities fraud.¹³⁰ In response, the court clarified its position that the parties' occupations demonstrated their ability to make and take delivery and the inherent value of the grain to them, and it was this fact that evidenced the actual delivery obligation under the HTAs.¹³¹

Schewe next asserted that the court improperly concluded that a farmer necessarily had the ability to deliver under the HTAs because "any number of factors could have eliminated [a farmer's] ability to make delivery" between the time the contracts were written and the time when performance became due.¹³² In response, the court pointed out that the proper consideration was not whether the farmer would be "absolutely certain to deliver," but whether, by virtue of their occupations and engagement in the business, the parties were likely to intend actual delivery under the contract.¹³³ In support of this point, the court reasoned that even cash forward contracts would be subject to regulation if the absolute certainty of delivery was the consideration.¹³⁴

B. Critical Analysis

The district court properly limited its analysis to the facts and arguments presented in the case.¹³⁵ Given the specific facts of the case and

129. *See id.* at 857.

130. *See id.* (reviewing Schewe's assertions).

131. *See id.* (stating that Schewe's assertions ignore plain language of contracts).

132. *Id.* at 857-58 (alteration in original) (citing Defendant's Reply Memorandum at 3, *Top of Iowa*, 6 F. Supp. 2d at 843 (No. C 96-3146-MWB)).

133. *See id.* at 858 (expanding issue to whether "they would be likely to produce and deliver").

134. *See id.* (noting that even cash forward contracts could not meet certainty requirement).

135. *See id.* at 846 (recognizing court's analysis may differ in each case because HTAs may differ from case to case); Iavarone, *supra* note 5, at 393 (asserting that inquiry into validity of HTAs is "a factual question that frequently depends on the course of dealing between the parties . . . [and] must proceed on an elevator by elevator process"). Limited as it was to the specific facts of the case, the court was not required to deal with other possible situations in which the current tests would be of little help. One such case involves a farmer who has produced grain in the past, but only to feed livestock. *See id.* at 396 n.94 (citing Complaint and Notice of Hearing at 6-7, *In re Grain Land Coop.*, 978 F. Supp. 1267 (D. Minn. 1997) (No. 3-96-1209) (alleging elevator entered HTAs with hog farmers who grew grain to feed hogs)). Although engaged in the business of producing the underlying commodity, he may not truly have had the requisite intent to deliver. *See id.* Other cases involve farmers who enter HTAs with elevators for quantities significantly beyond their ability to produce and deliver in any one or two years. *See Johnson v. Land O'Lakes, Inc.*, 18 F. Supp. 2d 985, 990-92 (N.D. Iowa 1998) (recognizing as undisputed fact that farmers with combined annual production capacity of 125,000 bushels of corn committed over 440,000 bushels of corn to HTAs under multiyear

the considerations established by precedent as the proper guidelines for determining whether contracts come within the cash forward exclusion, the court's analysis and ruling were appropriate.¹³⁶ The parties involved appear to be the quintessential parties to a cash forward contract.¹³⁷ Furthermore, significant evidence was presented to satisfy the prevailing test for validity, namely that the parties expected actual delivery of the physical commodity under the contract.¹³⁸

The facts of *Top of Iowa* tend to satisfy the dual requirements of subjective intent and objective delivery obligation as set forth in *Bybee*.¹³⁹ Schewe expressed his intent to deliver on more than one occasion.¹⁴⁰ Although the HTAs did not set a specific delivery date, the general expectation of delivery was implicit in the use of such terms as "arrival period" and "designated arrival period" and the phrase "[t]his is NOT considered a credit sale contract as long as final price is determined before delivery."¹⁴¹

Certain aspects considered to be characteristic of futures contracts were also missing.¹⁴² The parties never attempted to nullify the delivery obligation through offsetting transactions, aside from rolling the contracts.¹⁴³ In addition, *Top of Iowa* was an elevator engaged in the business of buying and selling grain, and Schewe was a grain producer.¹⁴⁴ The

program); Iavarone, *supra* note 5, at 390 n.75 (citing Complaint, *Gunderson v. ADM Investor Servs., Inc.*, 976 F. Supp. 818, 820-21 (N.D. Iowa 1997) (No. C 96-3148-MWB) (alleging 54 farmers with combined yearly production of 3,579,000 bushels committed 8,353,000 bushels of corn to HTAs)). Although they may satisfy the established criteria, they may have no actual intent to deliver, or the intent to deliver may be secondary to a more immediate speculative purpose. See *Land O'Lakes*, 18 F. Supp. 2d at 990-92 (acknowledging farmers' commitments under HTAs exceeded production capacity).

136. For a discussion of the principal cases dealing with the cash forward exclusion, see *supra* notes 79-105 and accompanying text. For a discussion of the court's analysis and holding in *Top of Iowa*, see *supra* notes 117-34 and accompanying text.

137. For a discussion of the relationship between the parties' business and the original purpose of the cash forward exclusion, see *infra* notes 144-46, *supra* note 34 and accompanying text.

138. For a discussion of the role that the delivery obligation plays in a judicial determination of whether contracts satisfy the cash forward exclusion, see *supra* notes 40-42 and accompanying text. For a discussion of the evidence tending to establish Schewe's intent to deliver under the contracts, see *supra* note 122 and accompanying text.

139. See *In re Bybee*, 945 F.2d 309, 313 (9th Cir. 1991).

140. For a discussion of delivery issues and Schewe's expressions of intent to deliver, see *supra* note 122 and accompanying text.

141. *Top of Iowa Coop. v. Schewe*, 6 F. Supp. 2d 845, 847-48 (N.D. Iowa 1998).

142. For a discussion of the characteristics of futures contracts, see *supra* notes 79-105 and accompanying text.

143. See *Top of Iowa*, 6 F. Supp. 2d at 847-49 (describing parties' conduct with regard to HTAs in question).

144. See *id.* at 847 (describing background of parties).

parties were capable of making and taking delivery, and the underlying grain had inherent value to them.¹⁴⁵ Considering that the cash forward exclusion was designed specifically to protect commodities producers and dealers carrying out their normal transactions from the burdens and interference of regulation, the parties were the quintessential parties to a legitimate cash forward contract.¹⁴⁶

The court, however, did not address a number of other issues. For instance, what did the language in the HTAs' second paragraph stating that "BUYER confirms the following futures transaction was made for seller today on the Chicago Board of Trade" mean?¹⁴⁷ This language could indicate that the HTA is merely a thinly veiled attempt to disguise a futures contract and bypass the exchange trading requirement of the CEA.¹⁴⁸ When the farmer or the elevator makes a futures transaction on its own account, either party can be seen as hedging its position vis-à-vis the underlying grain contract.¹⁴⁹ When, as here, the elevator makes the transaction on the farmer's behalf, it raises the suspicion that the elevator is using the HTA as a means of providing a futures brokerage service to the farmer.¹⁵⁰ Here, this view is strengthened because the HTAs in ques-

145. See *id.* at 855-56; *Commodity Futures Trading Comm'n v. Co Petro Mktg. Group, Inc.*, 680 F.2d 573, 578 (9th Cir. 1982) (citing H.R. REP. NO. 93-975, at 129-30 (1974) (describing parties for whom commodity in contract has "inherent value"))).

146. For a discussion of the history of the cash forward exclusion, see *supra* note 34 and accompanying text.

147. *Top of Iowa*, 6 F. Supp. 2d at 847.

148. See Iavarone, *supra* note 5, at 397-98 (arguing that elevators initiating futures contracts on farmers' behalf act like "Futures Commission Merchants," "accepting orders for commodity futures contracts and extending credit"); see also KOLB, *supra* note 6, at 51 (defining Futures Commission Merchant as "a firm or individual that accepts orders to trade futures on behalf of another party and who accepts money to support such an order").

149. See *Board of Trade v. Christie Grain & Stock Co.*, 198 U.S. 236, 249 (1905) (describing hedging as means of using futures market to reduce risk of position in market for commodity); KOLB, *supra* note 6, at 25 (defining hedging); Solomon & Dicker, *supra* note 8, at 199 (same); Cole, *supra* note 5, at 246 (same). Hedgers are often directly involved in trading the underlying commodity. See *Board of Trade*, 198 U.S. at 249 (describing hedging as means by which grain merchants protect against price fluctuations); KOLB, *supra* note 6, at 6 (asserting hedgers are often involved in producing and using underlying commodity); Solomon & Dicker, *supra* note 8, at 199 (same). In a typical hedge, a party with a long position in the underlying commodity would take a corresponding short position in the futures market for the same commodity. See KOLB, *supra* note 6, at 25-26 (discussing typical hedge transaction); Solomon & Dicker, *supra* note 8, at 199 & n.67 (same); Cole, *supra* note 5, at 246 (same). If the price of the underlying commodity drops, the loss will be offset by a gain in the short futures position. See KOLB, *supra* note 6, at 25-26 (discussing typical hedge transaction); Solomon & Dicker, *supra* note 8, at 199 & n.67 (same). This relationship enables hedgers to reduce their price risk, effectively locking in prices well in advance of harvest or delivery. See KOLB, *supra* note 6, at 25 (describing how hedgers reduce their price risk); Solomon & Dicker, *supra* note 8, at 199 & n.67 (same).

150. See *Top of Iowa*, 6 F. Supp. 2d at 847 (indicating that elevator made futures transaction on Schewe's behalf); see also KOLB, *supra* note 6, at 27 (noting that

tion made no explicit reference to any delivery obligation, but addressed aspects of the futures transactions in detail and assigned profits and losses on the futures transactions to the farmer.¹⁵¹

The problem with this argument is that, while Top of Iowa may have been providing brokerage-like services, it was not operating exactly like a typical brokerage.¹⁵² Significantly, the HTAs assigned responsibility for commissions and margin requirements to the elevator.¹⁵³ Normally, brokerages do not cover such costs for their clients.¹⁵⁴ It is likely that Top of Iowa did so under these HTAs in an effort to compete for their customers' grain business.¹⁵⁵ In addition, the HTAs imply and Schewe expressed directly a general understanding that the underlying grain eventually would be delivered.¹⁵⁶ Typical brokerages have no interest in whether grain is ever delivered on the futures transactions they execute.¹⁵⁷ In fact, most brokerages are strictly financial intermediaries and have neither the ability

customer gains access to trading directly through broker); Iavarone, *supra* note 5, at 397-98 (asserting that elevators taking futures positions on behalf of farmers act as Futures Commission Merchants); Asklesen, *supra* note 5, at 124-25 (stating elevators not only act as brokers and earn income from trading futures contracts for farmers, but also exercise certain competitive advantages over brokers who are subject to risk disclosure requirements and are prohibited from absorbing customers' margin calls).

151. See *Top of Iowa*, 6 F. Supp. 2d at 848 (indicating responsibility for margin calls and commissions was assigned to elevator under HTA with Schewe). Although the facts do not indicate that losses on the futures transactions were to be passed through to Schewe under the HTAs, such is usually the case. See Cole, *supra* note 5, at 246-47 (noting farmers commonly assume responsibility for gains or losses from futures transactions under HTAs).

152. See KOLB, *supra* note 6, at 6 (distinguishing between hedgers, who often are producers or users of commodities, and brokers, who typically only execute trades).

153. See *Top of Iowa*, 6 F. Supp. 2d at 848 (indicating that elevator assumed responsibility for margin calls and commissions).

154. See KOLB, *supra* note 6, at 11-13 (discussing operation of margin system in futures markets and indicating that traders, not brokers, are generally responsible for margin requirements). In fact, when a trader fails or refuses to post required margin amounts, the broker normally will close the trader's account. See *id.* (describing results of trader's failure to meet margin requirements). But see Asklesen, *supra* note 5, at 125 (asserting that elevators earn income from executing futures transactions for farmers and that ability to absorb margin calls is competitive advantage that elevators have over futures brokers).

155. See Memorandum of Law in Opposition to Plaintiff's Motion for Partial Summary Judgment at 9, *Top of Iowa*, 6 F. Supp. 2d at 843 (No. C-96-3146-MWB) (characterizing speculative features of HTAs as "misguided attempt [by elevators] to outdo each other in a race to capture market share by any means necessary"); see also Iavarone, *supra* note 5, at 374-75 (noting origins of HTAs in competition among grain elevators). But see Asklesen, *supra* note 5, at 124-25 (discussing elevators' advantages over brokerages in competition for farmers' futures transactions).

156. For a discussion of the delivery obligation under the HTAs in question and the parties' intent to carry it out, see *supra* notes 119-22 and accompanying text.

157. See KOLB, *supra* note 6, at 6 (distinguishing between hedgers and brokers).

nor the desire to accept grain deliveries.¹⁵⁸ Thus, although Top of Iowa's HTAs offered Schewe access to the futures market, it does not necessarily follow that the HTAs were intended solely as a means of eluding CFTC oversight of speculative futures transactions.¹⁵⁹ Nevertheless, the futures transaction on the farmer's behalf leaves a strong impression that the contract may have been intended to provide the farmer with speculative opportunities.¹⁶⁰

Another issue the court did not adequately address is the degree to which Top of Iowa's HTAs contain predetermined, standardized terms.¹⁶¹ This is important because standardization facilitates offsetting transactions that nullify the delivery obligation.¹⁶² Standardized terms raise the suspicion that the HTAs are really futures contracts.¹⁶³ In other cases dealing with the cash forward exception, the courts have specified standardization as a characteristic of futures contracts and individually negotiated terms as a hallmark of cash forward contracts.¹⁶⁴

The court also stated without further analysis that Top of Iowa's HTAs "involve[d] individually negotiated terms."¹⁶⁵ These HTAs, however, were preprinted forms with blank spaces to be filled in by the parties.¹⁶⁶ The blank spaces were filled in with information pertaining to specific futures contracts available on the Chicago Board of Trade.¹⁶⁷ Assuming Schewe

158. *See id.*

159. For a discussion of the evidence indicating that the parties intended to transfer the actual underlying grain, see *supra* notes 122-24, 138-41 and accompanying text.

160. For a discussion of the possibility that elevators use HTA contracts as a means of providing brokerage services to farmers, see *supra* notes 150-59 and accompanying text.

161. For a discussion of the extent to which the terms of the HTAs in question were nonnegotiable, see *supra* notes 106-09, *infra* notes 165-69 and accompanying text.

162. *See, e.g.,* Commodity Futures Trading Comm'n v. Co Petro Mktg. Group, Inc., 680 F.2d 573, 580 (9th. Cir 1982) (stating standardization of contracts facilitates offsetting, which is essential because investors rarely take delivery) (citing H.R. REP. NO. 93-975, at 129 (1974)).

163. *See In re First Nat'l Monetary Corp.*, [1982-1984 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 21,707, at 26,780 (CFTC Apr. 29, 1983) (determining cash forward exclusion did not apply to contract, in part because of standardization and lack of individually negotiated terms); *In re Stovall*, [1977-1980 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 20,941, at 23,777 (CFTC Dec. 6, 1979) ("Commodity futures transactions involve standardized contracts . . ."); Characteristics Distinguishing Cash and Forward Contracts and "Trade" Options, 50 Fed. Reg. 39,656, 39,658 (1985) (noting that forward contracts are frequently not standardized).

164. *See Salomon Forex, Inc. v. Tauber*, 8 F.3d 966, 971 (4th Cir. 1993) (distinguishing between standardized futures contracts and individually negotiated cash forward contracts); *Co Petro*, 680 F.2d at 580 (referring to "classic elements of a standardized futures contract").

165. *Top of Iowa Coop v. Schewe*, 6 F. Supp. 2d 843, 855 (N.D. Iowa 1998).

166. *See id.* at 847-48 (providing example of form of contract that Schewe entered into with Top of Iowa).

167. *See id.* at 848 (laying out document).

knew the approximate quantity and delivery month he desired, most of the remaining terms were set by the corresponding futures contract.¹⁶⁸ The only term open to negotiation was the delivery destination, which could be rendered moot by an offsetting transaction.¹⁶⁹

Schewe's HTAs, in fact, were somewhat similar to the Agency Agreements found to be futures contracts in *Co Petro*.¹⁷⁰ Like Top of Iowa Cooperative, the broker in *Co Petro* was engaged in the business of buying and selling the underlying commodity (petroleum products).¹⁷¹ As with Schewe's HTAs, *Co Petro*'s Agency Agreements were capable of offset because most of the terms were predetermined and standardized.¹⁷²

Standardization, however, is not a dispositive characteristic of futures contracts.¹⁷³ The delivery obligation in a standardized contract may be every bit as binding as an individually negotiated contract.¹⁷⁴ Other factors, particularly the parties' course of performance under the contracts, can give a clearer indication of actual intent.¹⁷⁵ For instance, although the customers in *Noble Metals* were ostensibly required to receive delivery,

168. See Plaintiff's Exhibit A, Hedge To Arrive Contract between Schewe and Top of Iowa, *Top of Iowa* (No. C 96-3146-MWB) (demonstrating that handwritten entries essentially correspond to details of futures contracts). For a discussion of how the terms of HTA contracts are generally established, see *supra* note 51 and accompanying text.

169. See Plaintiff's Exhibit A, Hedge To Arrive Contract between Schewe and Top of Iowa, *Top of Iowa*, 6 F. Supp. 2d at 843 (No. C 96-3146-MWB) (demonstrating that most handwritten entries are based on details of futures contracts).

170. See *Commodity Futures Trading Comm'n v. Co Petro Mktg. Group, Inc.*, 680 F.2d 573, 580-81 (9th Cir. 1982) (finding standardized Agency Agreements were futures contracts). In both cases, contract prices tracked the then-prevailing market prices, delivery dates were relatively predetermined and the contract quantities were multiples of standard units. See *Top of Iowa*, 6 F. Supp. 2d at 847-48 (describing details of HTAs between Schewe and Top of Iowa); *Co Petro*, 680 F.2d at 580-81 (describing details of *Co Petro*'s Agency Agreements).

171. See *Top of Iowa*, 6 F. Supp. 2d at 855 (describing business in which broker is engaged); *Co Petro*, 680 F.2d at 576 (describing *Co Petro* as "a broker of petroleum products").

172. For a comparison of the characteristics of the HTAs and *Co Petro*'s Agency Agreements, see *supra* note 170 and accompanying text. For a discussion of the roll of standardized contract terms in facilitating offset transactions, see *supra* notes 27-31 and accompanying text.

173. See *In re Bybee*, 945 F.2d 309, 312-15 (9th Cir. 1991) (deciding that, although contracts were sufficiently standardized to constitute futures contracts, exchange trading requirement did not apply because Bybee and supplier retained right to enforce delivery obligation).

174. See *id.* (holding contracts that were sufficiently standardized to be futures contracts nevertheless satisfied cash forward exclusion because of enforceable delivery obligation).

175. See *In re Stovall*, [1977-1980 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 20,941, at 23,779 (CFTC Dec. 6, 1979) (observing that only one customer ever fulfilled delivery obligation and stating that "this lack of delivery is the clearest indication that the contracts were not" cash forward contracts).

few ever did.¹⁷⁶ The parties eventually offset nearly every contract through third party transactions.¹⁷⁷ By contrast, Schewe's HTAs were capable of offset, but neither party ever nullified the delivery obligations that way.¹⁷⁸ As noted previously, Schewe himself indicated that he expected and intended eventually to deliver the grain.¹⁷⁹ Thus, although it may be possible to take issue with the court's assessment that the terms of the HTAs were individually negotiated, the parties' course of performance under the HTAs still supports the view that the contracts carried a bona fide delivery obligation.¹⁸⁰

The court also did not examine whether rolling effectively eliminates the delivery obligation, as rolling may not be truly permissive.¹⁸¹ The court justified rolling as an acceptable practice on the grounds that it was done as a matter of the elevator's permission, not as a contractual obligation.¹⁸² If, as Schewe asserted, permitting farmers to roll HTAs is the re-

176. See *Commodity Futures Trading Comm'n v. Noble Metals Int'l, Inc.*, 67 F.3d 766, 769, 773 (9th Cir. 1995) (describing customers' requirements under contracts for receipt and delivery of metals).

177. See *id.* at 769 ("Instead of taking physical delivery, however, the customers would contract for the third party to receive, and then sell, the metal.").

178. See *Top of Iowa Coop. v. Schewe*, 6 F. Supp. 2d 843, 847-49 (N.D. Iowa 1998) (describing parties' course of performance under HTAs in question). Even though Top of Iowa permitted Schewe to roll the HTAs, rolling only defers the delivery date. See *id.* at 848 (same). For a discussion of the mechanics and effect of rolling futures contracts months under HTAs, see *supra* notes 53-73 and accompanying text.

179. See *Top of Iowa*, 6 F. Supp. 2d at 855 (discussing Schewe's intention to make actual delivery). For a discussion of the significance of Schewe's statements, see *supra* note 122 and accompanying text.

180. For a discussion of the evidence indicating the parties intended actual physical transfer of the underlying grain, see *supra* notes 122-24, 138-41 and accompanying text.

181. See *Top of Iowa*, 6 F. Supp. 2d at 856 (holding that lack of express provision dealing with rolling indicated rolling was matter of elevator's discretion). The same court previously addressed the issue of whether rolling eliminates the delivery obligation in *Oeltjenbrun v. CSA Investors, Inc.*, 3 F. Supp. 2d 1024, 1043-44 (N.D. Iowa 1998). In *Oeltjenbrun*, the court viewed rolling as even less characteristic of futures contracts than bookout agreements because rolling does not extinguish the delivery obligation. See *id.* (comparing rolling transactions to bookout agreements). In both cases, the courts assumed the elevators' ability to refuse to roll. See *Top of Iowa*, 6 F. Supp. 2d at 856 (asserting elevator's lack of contractual obligation to execute roll transactions); *Oeltjenbrun*, 3 F. Supp. 2d at 1043 (same). Significantly, the district court has acknowledged explicitly the inherent speculative side of these transactions. See *id.* at 1044 (asserting rolling increases risk and allows farmer to speculate on price of grain, but "does not negate the nature of these contracts as contracts for actual physical delivery of grain").

182. See *Top of Iowa*, 6 F. Supp. 2d at 856 (determining that "the agreements to roll Schewe's contracts were separate, individually negotiated, new agreements" executed by Top of Iowa's permission, not as matters of obligation). Admittedly, the HTAs made no mention that Top of Iowa was in any way obligated to roll Schewe's contracts. See *id.* at 847-48 (describing HTAs between Schewe and Top of Iowa). The parties' performance under the contracts, however, may indicate their expectations better than the written terms of the contracts. See *Noble Metals*, 67 F.3d at 769, 772 (asserting parties' true expectation under contracts was evident in

sult of elevators trying to capture greater market share, then market pressures may make rolling a required feature of HTA contracts.¹⁸³ Grain elevators that do not permit rolling would risk losing business to elevators that do.¹⁸⁴ If this is the case, it weakens the court's comparison to the bookout agreements.¹⁸⁵ Courts permit bookout agreements in recognition of the reasonable need, in certain circumstances, to renegotiate or even cancel the delivery terms of cash forward contracts.¹⁸⁶ When renegotiation, either through rolling or offsetting transactions, becomes the rule rather than the exception, however, the inference grows that the parties are engaged in price speculation rather than normal hedging.¹⁸⁷

pattern of failure to perform delivery obligations even though written terms of contracts explicitly required delivery and prohibited offsetting). For a discussion of the suspicion with which courts and other observers have examined the written terms of similar contracts, see *supra* notes 100-01 and accompanying text.

If Top of Iowa was actually bowing to market pressures in allowing Schewe to roll and not simply making an exception for a customer in need, then rolling may have been an unwritten but presumed feature of the contracts. For a further discussion of elevators' alleged business objectives and incentives in rolling farmers' HTAs, see *supra* notes 148, 154-55 and accompanying text. To the extent that Top of Iowa was economically (if not legally) obliged to roll Schewe's HTAs, such an arrangement would still represent strong evidence that the HTAs were intended as a means of speculating in the futures market. See *Noble Metals*, 67 F.3d at 769, 772-73 (determining that, despite contract terms explicitly requiring delivery and prohibiting offsets, contracts were futures contracts based on parties' failure to perform delivery obligations).

183. See Memorandum of Law in Opposition to Plaintiff's Motion for Partial Summary Judgment at 9, *Top of Iowa*, 6 F. Supp. 2d at 843 (No. C 96-3146-MWB) (asserting speculative features of HTAs offered as "misguided attempt [by elevators] to outdo each other in a race to capture market share by any means necessary").

184. See *id.* (implying market pressures make permitting rolling nearly obligatory). For a discussion of the role of other HTA features as a possible advantage elevators hold over commodity brokerages in competing for farmers' futures trading business, see *supra* notes 154-55 and accompanying text.

185. See *Top of Iowa*, 6 F. Supp. 2d at 856 (predicating comparison to bookout agreements on lack of contractual obligation in original written HTAs requiring elevator to execute rolls); *Oeltjenbrun*, 3 F. Supp. 2d at 1043 (same).

186. See *In re Bybee*, 945 F.2d 309, 314-15 (9th Cir. 1991) (holding that contracts settled through bookout agreements, as opposed to delivery, were still within cash forward exclusion); Regulation of Hybrid Instruments, *supra* note 96, at 47,023 (recognizing parties entering contracts with enforceable delivery obligations and contemplating delivery may be unable to determine at time of entering contract whether delivery will be necessary); Statutory Interpretation, *supra* note 96, at 39,189-91 (asserting CFTC regulatory scheme should not apply to transactions with enforceable delivery obligations in which "delivery is deferred for reasons of commercial convenience or necessity").

187. See *Noble Metals*, 67 F.3d at 772-73 (relying on widespread disregard of delivery obligations to determine contracts were futures contracts).

V. IMPACT

In the final analysis, HTAs obviously do not fit neatly into either category—futures or cash forward contracts.¹⁸⁸ In form and function they satisfy the criteria of both cash forward and futures contracts.¹⁸⁹ They are far more speculative than ordinary cash forward contracts, yet they generally carry a meaningful delivery obligation.¹⁹⁰ The courts that have addressed the issue have seized on this delivery obligation in holding that HTAs meet the requirements of the cash forward exclusion.¹⁹¹ Although some courts have recognized the inherent speculative nature of HTAs, they have not expressed concern for the impact of this characteristic.¹⁹²

188. See Iavarone, *supra* note 5, at 393-99 (discussing whether HTAs are cash forward or futures contracts); Asklesen, *supra* note 5, at 125 (noting legality of HTAs is difficult to determine due to significant variations); Cole, *supra* note 5, at 254-55 (discussing legality of HTAs).

189. See *Johnson v. Land O'Lakes, Inc.*, 18 F. Supp. 2d 985, 992 (N.D. Iowa 1998) (noting that like cash forward contracts, HTAs can be, and frequently have been, used to transfer ownership of grain); *Oeltjenbrun*, 3 F. Supp. 2d at 1046 (noting farmers had previously delivered grain under HTAs). Like futures contracts, however, HTAs can be used for purposes of speculating directly on regulated futures exchanges on price changes in the underlying commodity. See Iavarone, *supra* note 5, at 393-99 (discussing futures-like aspects of HTAs); Asklesen, *supra* note 5, at 123-25 (describing HTAs and discussing elevators' competition with commodity brokers); Cole, *supra* note 5, at 254-55 (noting some HTAs may be found to be illegal off-exchange futures); see also *CFTC Interpretative Statement*, *supra* note 53, at 43,851-52 (declining to determine status of HTA contracts with respect to cash forward exclusion, but enumerating contract features consistent with "prudent risk-reduction"). Some HTAs even carry buyout provisions that enable parties to cancel the delivery obligation by making a cash payment. See *Land O'Lakes*, 18 F. Supp. 2d at 992 (stating farmers asserted, and elevator did not dispute, that contracts included buyout provision).

190. See *Land O'Lakes*, 18 F. Supp. 2d at 997 (holding HTAs in question were contracts on which parties contemplated and intended actual delivery); *Barz v. Geneva Elevator Co.*, 12 F. Supp. 2d 945, 954 (N.D. Iowa 1998) (same); *Andersons, Inc. v. Crotser*, 7 F. Supp. 2d 931, 936 (W.D. Mich. 1998) (same); *Top of Iowa*, 6 F. Supp. 2d at 856 (same); *Oeltjenbrun*, 3 F. Supp. 2d at 1044 (same); *In re Grain Land Coop.*, 978 F. Supp. 1267, 1277 (D. Minn. 1997) (same); *Countrymark Coop., Inc. v. Smith*, No. 5-97-21, 1997 WL 762813, at *8 (Ohio Ct. App. Dec. 8, 1997) (same).

191. See *Land O'Lakes*, 18 F. Supp. 2d at 997 (holding HTAs in question were valid cash forward contracts because parties contemplated and intended actual delivery); *Barz*, 12 F. Supp. 2d at 954 (same); *Crotser*, 7 F. Supp. 2d at 936 (same); *Top of Iowa*, 6 F. Supp. 2d at 856, 858 (same); *Oeltjenbrun*, 3 F. Supp. 2d at 1044 (same); *Grain Land Coop.*, 978 F. Supp. at 1277 (same); *Countrymark*, 1997 WL 762813, at *8 (same).

192. See *Land O'Lakes*, 18 F. Supp. 2d at 997 (ruling farmer's asserted belief that HTAs were intended for speculating did not alter nature of HTAs as contracts for physical delivery of grain); *Oeltjenbrun*, 3 F. Supp. 2d at 1044 (asserting that rolling does not negate nature of HTAs as contracts for physical delivery of grain, despite raising risk and allowing producer to speculate); *Grain Land Coop.*, 978 F. Supp. at 1277 (asserting that rolling introduces imprudent risk, but does not detract from contract's principal purpose as marketing tool).

HTAs pose such analytical difficulties because they were intended to be speculative instruments as well as a means of passing title.¹⁹³ They exhibit aspects of cash forward and futures contracts because they were designed to serve the underlying purposes of both instruments.¹⁹⁴ HTAs carry delivery obligations because the parties generally do intend to pass title to the grain.¹⁹⁵ HTAs also represent greater speculative opportunities because the parties intend that as well.¹⁹⁶ The economic reality is that grain producers today are looking for newer, more flexible instruments that they can use to sell their crops and still take advantage of other profitable opportunities that may arise.¹⁹⁷ HTAs are a logical result of the need for hybrid instruments that provide grain producers with means to manage risk while maximizing their opportunities in a volatile market.¹⁹⁸

The likely outlook for the foreseeable future is that the legal and economic situations will remain unsettled.¹⁹⁹ No cases have yet reached the

193. See *Land O'Lakes*, 18 F. Supp. 2d at 997 (holding that HTAs in question were contracts on which parties contemplated and intended actual delivery, even though farmer asserted belief that purpose of HTAs was speculation); *Barz*, 12 F. Supp. 2d at 954 (holding HTAs were contracts for delivery of grain); *Crotser*, 7 F. Supp. 2d at 936 (same); *Top of Iowa*, 6 F. Supp. 2d at 856 (same); *Oeltjenbrun*, 3 F. Supp. 2d at 1044 (same); *Grain Land Coop.*, 978 F. Supp. at 1277 (same); *Countrymark*, 1997 WL 762813, at *8 (same); see also Iavarone, *supra* note 5, at 390 (emphasizing that HTA serves only as means of speculation).

194. See Asklesen, *supra* note 5, at 122 (asserting HTAs were created as marketing tool); Cole, *supra* note 5, at 244 (stating farmers use HTAs as speculative means of obtaining highest price possible for grain).

195. See *Land O'Lakes*, 18 F. Supp. 2d at 997 (holding HTAs in question were contracts on which parties contemplated and intended actual delivery); *Barz*, 12 F. Supp. 2d at 954 (same); *Crotser*, 7 F. Supp. 2d at 936 (same); *Top of Iowa*, 6 F. Supp. 2d at 856 (same); *Oeltjenbrun*, 3 F. Supp. 2d at 1044 (same); *Grain Land Coop.*, 978 F. Supp. at 1277 (same); *Countrymark*, 1997 WL 762813, at *8 (same); see also Asklesen, *supra* note 5, at 122 (asserting HTAs were created as marketing tool).

196. See *Land O'Lakes*, 18 F. Supp. 2d at 997 (disregarding, but not contradicting, farmers' asserted belief that purpose of HTAs was speculation); see also Iavarone, *supra* note 5, at 390 (emphasizing HTA serves only as means of speculation); Cole, *supra* note 5, at 244 (stating farmers use HTAs as speculative means of obtaining highest price possible for grain).

197. See David C. Barrett, *Hedge-To-Arrive Contracts*, 2 DRAKE J. AGRIC. L. 153, 154 (1997) (asserting that political and economic developments create need for flexible hybrid contracts); Asklesen, *supra* note 5, at 138-39 (observing commodity price volatility will lead to development of other contracts similar to HTAs).

198. See Barrett, *supra* note 197, at 154 (discussing need for HTAs); Asklesen, *supra* note 5, at 139 (implying that development of HTAs and similar contracts is, in part, outgrowth of market volatility).

199. Compare *Land O'Lakes*, 18 F. Supp. 2d at 997 (holding as matter of law HTA was valid cash forward contract), with *CFTC Interpretative Statement*, *supra* note 53, at 43,851-52 (considering determination that certain HTAs are illegal). On the one hand, all of the courts that have addressed the issue so far have held, as a matter of law, that HTAs are valid cash forward contracts. See *Land O'Lakes*, 18 F. Supp. 2d at 997 (holding HTAs in question were valid cash forward contracts because parties contemplated and intended actual delivery); *Barz*, 12 F. Supp. 2d at 954 (same); *Crotser*, 7 F. Supp. 2d at 936 (same); *Top of Iowa*, 6 F. Supp. 2d at 856, 858 (same); *Oeltjenbrun*, 3 F. Supp. 2d at 1044 (same); *Grain Land Coop.*, 978 F. Supp. at 1277 (same); *Countrymark*, 1997 WL 762813, at *8 (same). On the other

circuit court level, so no decisions have binding precedential value outside of their immediate districts. Although most decisions that have reached the merits have held that HTAs are valid cash forward contracts, only a few such cases have been reported overall, and these cases have presented little variation in terms of arguments and relevant facts.²⁰⁰

Some argue that cash forward contracts and simple HTAs provide farmers with sufficient downside price protection and that the only advantage of newer HTAs is that they give the farmer greater speculative opportunities.²⁰¹ As a result, courts should consider HTAs futures contracts subject to the exchange-trading requirement of the CEA.²⁰² Proponents of regulation, however, are likely to meet with frustration as long as they advocate application of the existing concepts.²⁰³ Courts attempting to fit HTAs into one category or the other will continue to determine that the HTAs are cash forward contracts because the prevailing test is predicated

hand, the CFTC may be leaning toward a determination that HTAs with certain features or administered in certain ways are illegal off-exchange futures contracts. See *CFTC Interpretative Statement*, *supra* note 53, at 43,851-52 (discussing practices consistent with prudent risk-reduction); see also Barrett, *supra* note 197, at 172-73 (discussing HTA features and practices likely to invalidate contracts).

In addition, grain markets are likely to face more volatility in the future. See *id.* at 178 (implying that changes in government farm policy will lead to greater volatility); Asklesen, *supra* note 5, at 126 (discussing market forces resulting in price volatility in 1995-96). Furthermore, it would be unwise to ignore the possibility of a reoccurrence of the market factors blamed for the 1995-96 price rise, such as changes in government farm policies, a large corn processing industry with a relatively inelastic demand for corn, the growth of large hog production systems with a relatively inelastic demand for corn and global policy changes. See *id.* (discussing market forces influencing volatility in corn market).

200. See *Land O'Lakes*, 18 F. Supp. 2d at 992, 997 (holding HTAs between grain buyers and sellers were valid cash forward contracts, even though amount of grain committed exceeded farmers' annual production and farmers asserted that intent of contracts was to speculate); *Barz*, 12 F. Supp. 2d at 954, 957 (holding HTAs between grain buyers and producers, even though rolled, were valid cash forward contracts); *Crotser*, 7 F. Supp. 2d at 936 (holding HTAs between grain elevator and farmer that contained explicit roll provisions were valid cash forward contracts); *Top of Iowa*, 6 F. Supp. 2d at 858 (holding HTAs between grain buyers and producers, even though rolled, were valid cash forward contracts); *Oeltjenbrun*, 3 F. Supp. 2d at 1044 (same); *Grain Land Coop.*, 978 F. Supp. at 1277 (same); *Countryside*, 1997 WL 762813, at *8 (same).

201. See Iavarone, *supra* note 5, at 390 (emphasizing HTA serves only as means of speculation).

202. See *id.* at 397-99 (arguing certain HTA features and practices make them illegal off-exchange futures contracts).

203. See *Land O'Lakes*, 18 F. Supp. 2d at 996-97 (ruling that farmer's asserted belief that HTAs were intended for speculating did not alter nature of HTAs as contracts for physical delivery of grain); *Oeltjenbrun*, 3 F. Supp. 2d at 1044 (asserting rolling does not negate nature of HTAs as contracts for physical delivery of grain, despite giving rise to risk and allowing producer to speculate); *Grain Land Coop.*, 978 F. Supp. at 1277 (asserting rolling introduces imprudent risk, but does not detract from contract's principal purpose as marketing tool).

on the intent to deliver.²⁰⁴ Intent to deliver will usually be discernible as long as HTAs are designed, in part, to market grain.²⁰⁵

The best strategy for those seeking to regulate HTAs is to advocate reconsideration of the intent to deliver as a factor in distinguishing cash forward contracts from futures contracts.²⁰⁶ Their approach should be to remind the courts that the intent underlying commodities regulation was to curb excess speculation and price manipulation and also to argue that speculative instruments such as HTAs are not necessary given the availability of less-speculative instruments that adequately accomplish valid marketing objectives.²⁰⁷

The main problem with this proposed strategy is that it will require courts and legislatures to discard the traditional belief that it is possible to separate the everyday transactions incident to activities in the commodities markets from speculative activities typical of the futures markets.²⁰⁸ This strategy will also require those bodies to take the additional step of deciding that the need to regulate speculation is greater than the desire to protect commodity producers from regulation.²⁰⁹

In addition, regulating HTAs may be a somewhat heavy-handed response, considering that the parties usually are in the business of producing, selling and buying grain.²¹⁰ Presumably, they have some

204. See *Land O'Lakes*, 18 F. Supp. 2d at 996-97 (holding HTAs were contracts for physical delivery of grain despite farmers' asserted belief that contracts were for speculating); *Oeltjenbrun*, 3 F. Supp. 2d at 1044 (ruling that HTAs were valid cash forward contracts because parties contemplated and intended actual delivery, despite speculative nature of rolling); *Grain Land Coop.*, 978 F. Supp. at 1277 (same).

205. See *Land O'Lakes*, 18 F. Supp. 2d at 997 (holding HTAs in question were contracts on which parties contemplated and intended actual delivery); *Barz*, 12 F. Supp. 2d at 954, 957 (same); *Crotser*, 7 F. Supp. 2d at 936 (same); *Top of Iowa*, 6 F. Supp. 2d at 856 (same); *Oeltjenbrun*, 3 F. Supp. 2d at 1044 (same); *Grain Land Coop.*, 978 F. Supp. at 1277 (same); *Countrysmark*, 1997 WL 762813, at *8 (same); see also Asklesen, *supra* note 5, at 122 (asserting that HTAs were created as marketing tool).

206. For a discussion of the significance of the delivery obligation in determining the validity of deferred shipment contracts, see *supra* note 40 and accompanying text.

207. For a further discussion of the objectives of commodity futures markets regulation, see *supra* note 34 and accompanying text.

208. See *Commodity Futures Trading Comm'n v. Co Petro Mktg. Group, Inc.*, 680 F.2d 573, 577 (9th Cir. 1982) (discussing creation of cash forward exclusion as attempt to exempt "legitimate commercial transactions" from regulation aimed at curbing speculative abuses in futures trading).

209. See *Futures Trading Laws: Hearings Before the Senate Comm. on Agric., Nutrition and Forestry*, 104th Cong., 2d Sess. 1 (1996) (statement of Sen. Richard G. Lugar) (discussing dilemma of balancing need for maintaining public confidence in well-regulated marketplace and need to free marketplace from regulation for competitive purposes).

210. See *Land O'Lakes*, 18 F. Supp. 2d at 988 (observing contracts were between parties engaged in business of producing, selling and buying grain); *Barz*, 12 F. Supp. 2d at 945-46 (same); *Crotser*, 7 F. Supp. 2d at 932 (same); *Top of Iowa*, 6 F. Supp. 2d at 847 (same); *Oeltjenbrun*, 3 F. Supp. 2d at 1028 (same); *Brown v. North Cent. F.S., Inc.*, 987 F. Supp. 1150, 1151-52 (N.D. Iowa 1997) (same); *Grain Land*

understanding of the usual dynamics of their markets as well as the risks involved in speculative hedging.²¹¹ Investor education may be more in keeping with the recent trend of reducing the level of government involvement in the agricultural economy.²¹² As government involvement gives way to market forces, farmers will need the increased flexibility that instruments such as HTAs offer.²¹³ Farming is increasingly becoming more of a business than an occupation.²¹⁴ Those engaged in the business will best be able to succeed if they are allowed access to the tools they need and the training to use those tools properly.²¹⁵

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Coop., 978 F. Supp. at 1269 (same); *Gunderson v. ADM Investor Servs., Inc.*, 976 F. Supp. 818, 820 (N.D. Iowa 1997) (same); *Herwig v. Hahnman-Albrecht*, No. 96 C 6107, 1997 WL 72079, at *1 (N.D. Ill. Feb. 13, 1997) (same); *Eby v. Producers Cop., Inc.*, 959 F. Supp. 428, 430 (W.D. Mich. 1997) (same); *Farmers Co-operative Elevator v. Abels*, 950 F. Supp. 931, 932 (N.D. Iowa 1996) (same); *Hodge Bros. v. DeLong Co.*, 942 F. Supp. 412, 414 (W.D. Wis. 1996) (same); *Countrysmark*, 1997 WL 762813, at *8 (same); see also Barrett, *supra* note 197, at 177-78 (arguing governmental regulations restrain agriculture); Asklesen, *supra* note 5, at 122 (stating that regulation results in competitive disadvantages in form of increased costs and reduced flexibility of marketing instruments).

211. See Barrett, *supra* note 197, at 177-78 (asserting grain producers are becoming increasingly sophisticated in business matters).

212. See *id.* (arguing that changes in government farm policy create need for wide variety of flexible marketing and risk-management tools and education to maximize their benefits).

213. See *id.* (emphasizing need for more flexibility and wide variety of marketing and risk-management tools in wake of changes in farm policy).

214. See BUREAU OF THE CENSUS, U.S. DEP'T OF COMMERCE, STATISTICAL ABSTRACT OF THE UNITED STATES 1997 665-66, 668 (1997) (indicating following agricultural trends between 1982 and 1992: 14% decrease in total number of farms; 4% decrease in total amount of land in farms; and 10% increase in average size of farms; and following trends between 1987 and 1992: 8% decrease in number of family-owned farms and 9% increase in number of corporate-owned farms).

215. See Barrett, *supra* note 197, at 177-78 (arguing that grain producers need greater choice of more flexible financial tools as well as training to use those tools).

